BY CA VIMAL PUNMIYA

1. INTRODUCTION

Income – tax Act, 1961 (hereinafter referred to as 'The Act') is the only legislation of our country which refers 92 Central Acts and various State Legislations. To understand the various taxation issues relating to Real Estate Transactions, it is very essential to know the provisions of general law with special reference to Transfer of Property Act, Registration Act, Stamp Act, Development Control Regulations, etc. In this paper we have made an attempt to discuss some of the very important taxation issues relating to Real Estate Transactions. Mumbai is to suppose to be seventh biggest city in the world with beautiful coastal line. Mumbai is the commercial and financial capital of India and also a Gateway of International Trade and Industrial Development of India.

2. METHODS OF ACCOUNTING

a. PROJECT COMPLETION METHOD

A method of recognizing revenues and costs from a long-term project in which profit is recorded only when the project has been completed. Even if payments are received while the project is in progress, no revenues are recorded until its completion. The completed-contract method is a conservative way of accounting for long-term undertakings and is used for certain types of construction projects.

It is held that Recognition/identification of income under the Act, is attainable by several methods of accounting. It may be noted that the same result could be attained by any one of the accounting methods. Completed contract is one such method. Similarly, percentage of completion is another such method.

CIT v/s Bilahari Investments (P) Ltd. [(2008) 299 ITR 1 SC]

b. PERCENTAGE COMPLETION METHOD

A method of recognizing revenues and costs from a long-term project in relation to the percentage completed during the course of the project. Thus, the percentage-of-completion method allows a business profits (or losses) on a project before its completion.

It is held that Assessee-contractor having offered profits for tax on the basis of percentage completion method which is a standard accounting practice and has been constantly followed by the assessee in subsequent years, the same could not be rejected.

CIT vs. Advance Construction Co. (P) Ltd. [(2005) 275 ITR 30 (Guj.)]

c. CHANGE OF METHOD OF ACCOUNTING

Disclosure of changes in an accounting policy used for construction contracts should be made in the financial statements giving the effect of the change and its amount. However if a contractor changes from the percentage of completion method to the completed contract method for contracts in progress at the beginning of the year it may not be possible to quantify the effect of the change. In such cases disclosure should be made of the amount of attributable profits reported in prior years in respect of contracts in progress at the beginning of the accounting period.

It is held that the assessee having changed his method of accounting from work-in-progress in original return to project completion method in revised return, assessment had to be made as per revised return.

Satish H. Patel [93 TTJ 458 (Pune)]

3. DISCLOSURE IN THE COURSE OF SEARCH – WHETHER INCOME MUST BE TAXED ON COMPLETION OF THE PROJECT?

The conduct of search and seizure operation in a particular year does not lead to an inference that the undisclosed income detected as a consequence thereof has to be taxed in the assessment year relevant to the previous year in which search was conducted. In other words, accounting of profits has yet to be made on the basis of method of accounting followed by the assessee.

It is held that Undisclosed income in the form of 'on money' stood established by seizure of document r/w statement recorded under s. 132(4); however in computing undisclosed income, expenditure incurred has to be allowed; income discovered has to be taxed in assessment years as per method of accounting followed by assessee.

Dhanvarsha Builders & Developers (P) Ltd. vs. DCIT [(2006) 102 ITD 375 (Pune)]

4. FINANCE COST, INDIRECT COST AND COMPUNDING CHARGES.

A. INTEREST ON BORROWED CAPITAL – SCOPE OF SECTION 36(1)(iii)

The amount of the interest paid in respect of capital borrowed for the purposes of the business or profession is allowed as deduction.

[Provided that any amount of the interest paid, in respect of capital borrowed for acquisition of new asset for extension of existing business or profession (whether capitalised in the books of account or not); for any period beginning from the date on which the capital was borrowed for acquisition of the asset till the date on which such asset was first put to use, shall not be allowed as deduction.]

It is held that construction project undertaken by the assessee-builder constituted its stock-in-trade and the assessee was entitled to deduction under s. 36(1)(iii) in respect of interest on loan obtained for execution of said project.

CIT vs. Lokhandwala Construction, (2003) 260 ITR 579 (Bom)

It is held that the assessee following project-completion method of accounting, the interest identifiable with that project should be allowed only in the year when the project is completed and the income from that project is offered for taxation. The same cannot be deducted as period cost from year to year. True profits in such a case can be determined only when entire cost of the project, direct or indirect, including finance cost is added to the value of work-in progress.

Wallstreet Constructions Ltd. & Anr. Vs. JCIT 2006 101 ITD 156 (Mum) (SB)

It is held that even though assessee was following competed contract method for returning its income, its claim of finance cost as a period cost in nature of interest was allowable in the year in which it was incurred or accrued, in accordance with AS – 7 issued by the ICAI.
JCIT vs. Raheja (P) Ltd. (2006) 102 ITD 414 (Mum.)

B. ADVERTISEMENT EXPENSES TO BE CAPITALISED AS WORK-IN-PROGRESS
It is held that Assessee following project completion method, and advertisement expenses of the two projects being allocable to individual project, such advertisement expenses have to be capitalized as work – in – progress to be allowed deduction in the year of completion of project.
Income Tax Officer vs. Panchvati Developers [115 TTJ 139 (Mum)]

C. WHETHER COMPOUNDING CHARGES PAID BY BUILDERS ALLOWED AS A DEDUCTION
In this case it was held in the order passed by a competent authority of Town Planning in unmistakable terms stated that he had permitted the payment of compounding charges by erring builders to regularize the infirmity in the building construction. There could not be any doubt that what had been done was to permit the assessee to compound the offence committed by it putting up an unauthorized construction.

Explanation to Sec. 37(1) defines that any expenditure incurred for any purpose which is an offence or which is prohibited by law is not entitled to deduction. Hence compounding of the offence under Corporation Act cannot take away the rigour of explanation to sec 37 and the deduction is not available.
Mamta Enterprises – [135 Taxman 393 (Karnataka.)]

5. <u>PROPERTY V/S BUSINESS INCOME</u>

With several malls and business centers remerging taxability of rental income arising therefrom is an important issue. Supreme Court in **Shambhu Investment (P) Ltd. v. CIT (2003) 263 ITR 143 (SC)** has held that "*income derived from letting assessable as income from property and not business income. In this case assessee was letting out furnished premises on monthly rent basis to various parties along with furniture, fixtures, light, air - conditioners, etc., for being used as "table space*".
Under the agreement, the assessee is also providing services like watch and ward staff, electricity, water and other common amenities to the occupiers. These services are not separately charged. Entire cost of property already recovered by way interest – free advance by the assessee. Only intention was to let out the portion of premises to respective occupants. It was held that income derived from letting rightly held assessable as income from property and not business income.

It was held that income derived by assessee from shopping malls/business center was assessable as business income and not as income from house property. It held that "The fact that the apex court held that the income earned by Shambhu Investment (P) Ltd. is *assessable as property income has no relevance in the facts and circumstances of the present case. Because in that case facts showed that the main intention was to earn rental income. That was why the entire cost of the property was recovered from the tenants by way of interest – free advance. In the instant case, on the other hand, the assessee had taken bank loans to finance his projects like any other businessman. As discussed hereinabove, every action of the p-resent assessee appears to be with the sole object of commercial exploitation of the premises".*

PFH MALL AND RETAIL MANAGEMENT LTD. V. ITO(2008)110 ITD 337 (KOL.)

Letting out of all the rooms of a property, used as a guest house by the assessee to a bank to be used as a training centre was a part on running of the lodge business and, therefore, income from such leasing was assessable as business income and necessary income was assessable as business expenditure.

CIT V. PATESHWARI ELECTRICAL & ASSOCIATED INDUSTRIES (P) LTD. (2006) 282 ITR 61 (ALL.)

When property has been let out not only as property but with services which is a complex letting, the income cannot be said to be derived from mere ownership of house property but may be assessable as income from business. If the owner of a property carries on upon the property some activities which results in profits and gains arising, not from the ownership of the property but from the owners used thereof, letting various services to the tenants, those profits and gains may be chargeable under section 28 as Income from Business, apart from the assessment u/s 22 in respect of Income From House Property.

CIT V. SARABHAI (P) LTD. (2003) 263 ITR 197 (GUJ.)

6. INTEREST EARNED ON SURPLUS MONEY PARKED AS FIXED DEPOSIT WITH BANK TAXED UNDER THE HEAD THE BUSINESS.

It is held that advances from customers intending to purchase flats, deposit of surplus money with bank in course of business – the accrued interest arises out of business activities hence such interest income assessable as business income and not as income from other source.

CIT V. LOK HOLDINGS 308 ITR 356 (BOM.)

It is held that merely because the income has been assessed as business income, it will not automatically confer the benefit of a particular deduction once there is a rider provision that such income should be derived from a particular source.

TRICOM INDIA LTD V. ACIT, ITA NO. 1924/MUMBAI/08, ITAT MUMBAI BENCH E

7. CAPITAL GAIN vs. BUSINESS INCOME

Whether a particular asset is stock-in-trade or capital asset does not depend upon the nature of the article, but the manner in which it is held. The same item may be stock-in-trade in the hands of the assessee who deals in that item. But it will be capital asset in the case of an assessee who uses it for earning income or holds as an investment.

For example, a dealer in real estate holds a piece of land or house property as stock-in-trade. But it will be a capital asset in the hands of a person who holds it as an investment and derives income from leasing or renting of the property.

Even stock-in-trade may become capital asset in certain circumstances and *vice versa*. If an assessee who deals in certain goods or commodities as trader, on closure of the business, retains the existing stocks as investment, the stocks will become capital asset in his hands from the time of closure, notwithstanding that they were stock-in-trade earlier in his hands. Even in the course of a business, an assessee may try to transfer some of the stock-in-trade from his trading activity and decide to hold them as investment.

The stocks so held would assume the character of capital asset from the date of such holding. This may usually happen in the case of dealer in shares and real estate. But in all these cases, the finding will be one of fact depending upon the intention and conduct of the assessee supported by direct and circumstantial evidence. Similarly, when a capital asset is converted into stock-in-trade, the same will no longer be capital asset. However, this situation is covered by section 45(2).

The activity of an assessee in dividing the land into plots and not selling it as a single unit as he purchased, goes to establish that he was carrying on business in real property and it is a business venture.
RAJA J. RAMESHWAR RAO V CIT (1961) 42 ITR 179 (SC)

Ordinarily, where a person acquired land with a view to selling it later after developing it and actually divided the land into plots and sold the same in parcels, the activity could only be described as a business adventure. Generally speaking, the original intention of the party in purchasing the property, the magnitude of the transaction of purchase, the nature of the property, the length of its ownership and holding, the conduct and subsequent dealings of the assessee in respect of the property, the manner of its disposal and the frequency and multiplicity of transactions afforded valuable guides in determining whether the assessee was carrying on a trading activity and whether a particular transaction should be stamped with the character of a trading adventure.
CIT V TRIVEDI (V.A.) (1988) 172 ITR 95 (BOM)

However, on some different facts and circumstances. It was held that profit on the sale of land after plotting it out to secure better price cannot be taxed as profit from an adventure in the nature of trade. It shall be taxed under the head 'capital gain'.
CIT V SHASHI KUMAR AGRAWAL (2003) 131 TAXMAN 823 (ALL)

Assessee had purchased a plot of land in 1958. In view of the Urban Land (Ceiling and Regulation) Act, 1976, she applied for construction of group housing on the excess land and sold the land to a developer and builder. The Assessing Officer held that the installments received from the builder are business income. The Tribunal held that it is not business income as there was no adventure in the nature of trade. On reference, the Delhi

High Court upheld the decision of the Tribunal and held as under:
"The plot was purchased in the year 1958 and after the operation of law, namely, the Urban Land (Ceiling and Regulation) Act, 1976, it was not possible for the assessee to retain the land. It was very clear that on the assessee's part there was only an intention to transfer the land and not the portion that may be constructed by the builder on a future date. Clause 3 of the agreement merely provided the mode of payment. On the facts and in the circumstances of the case, the Tribunal was right in holding that there was no adventure in the nature of trade and thereby deleting business income of Rs. 11,87,387 from the income of the assessee."
CIT v Radha Bai (2005) 272 ITR 264 (Del)

Where some land, which was contributed by partners as capital and used as brick field and later given for development, upholding the finding of the Tribunal, it was held that the firm did not acquire the land, with a view to sell it at a profit. It was treated in the accounts as a fixed asset given to other for outright development without the assessee itself plotting it out, so that it had continued to be a capital asset. There was no scope, it was found, for holding it either as business or even an adventure in the nature of trade. ***CIT v Mohakampur Ice & Cold Storage (2006) 281 ITR 354 (All)***

What was necessary was to find out the intention of the assessee at the time of the purchase of land. Where the land was never purchased by the assessee. She acquired the same on the basis of a will on the death of her husband. She sold the same in parcels because the huge area could not be sold in one transaction. Such an activity could not amount to trade or business within the meaning of the Act.
CIT V SUSHILA DEVI JAIN (2003) 259 ITR 671 (P&H)

A company can hold shares as stock-in-trade for the purpose of doing business of buying and sale of such shares, while at the same time it can also hold other shares as its capital for the purpose of earning dividend income. Thus, where the finding was that the shares in question were never treated by the assessee as stock-in-trade and they were held for earning dividend only, it was held that the Tribunal was right in law in holding that the profit on sale of such shares was to be treated as capital gains.
CIT v N.S.S. Investments Pvt. Ltd. (2005) 277 ITR 149 (Mad)

Where it was an admitted position that the land in question was held as a capital asset by the assessee and not as a business asset and it had also been noticed that the assessee had relinquished the land in lieu of forest department allowing use of their land for laying down the drainage and the question was as to whether loss arising on such transfer could be allowed as a business loss, it was held that the loss arising on account of transfer of land to the forest department in lieu of the use of forest land for laying the drainage for discharge of effluent, was capital loss and could not be allowed as a business loss.
Shreyans Industries Ltd. v Jt. CIT (2005) 277 ITR 433 (P&H)

8. **80IB(10) [DEVELOPING AND BUILDING HOUSING PROJECTS[:**

The amount of deduction in the case of an undertaking developing and building housing projects approved before the 31st day of March, 2008 by a local authority shall be hundred per cent of the profits derived in the previous year relevant to any assessment year from such housing project if:

(a) Such undertaking has commenced or commences development and construction of the housing project on or after the 1st day of October, 1998 and completes such construction

(i) in a case where a housing project has been approved by the local authority before the 1st day of April, 2004, on or before the 31st day of March, 2008;

(ii) in a case where a housing project has been, or, is approved by the local authority on or after the 1st day of April, 2004 but not later than the 31st day of March, 2005, within four years from the end of the financial year in which the housing project is approved by the local authority.

(iii) in a case where a housing project has been approved by the local authority on or after the 1st day of April, 2005, within five years from the end of the financial year in which the housing project is approved by the local authority.

Explanation: For the purposes of this clause, -

- in a case where the approval in respect of the housing project is obtained more than once, such housing project shall be deemed to have been approved on the date on which the building plan of such housing project is first approved by the local authority;

- the date of completion of construction of the housing project shall be taken to be the date on which the completion certificate in respect of such housing project is issued by the local authority;

(b) The project is on the size of a plot of land which has a minimum area of one acre

(c) The residential unit has a maximum built-up area of one thousand square feet where such residential unit is situated within the cities of Delhi or Mumbai or within twenty-five kilometres from the municipal limits of these cities and one thousand and five hundred square feet at any other place;

(d) The built-up area of the shops and other commercial establishments included in the housing project does not exceed three per cent of the aggregate built-up area of the housing project or five thousand square feet, whichever is higher.

(e) Not more than one residential unit in the housing project is allotted to any person not being an individual; and

(f) in a case where a residential unit in the housing project is allotted to a person being an individual, no other residential unit in such housing project is allotted to any of the following persons, namely:--

(i) The individual or the spouse or the minor children of such individual,
(ii) The Hindu undivided family in which such individual is the karta,
(iii) any person representing such individual, the spouse or the minor children of such individual or the Hindu undivided family in which such individual is the karta;

IMPORTANT JUDICIAL PRONOUNCEMENTS:

- *One of the issue for consideration is whether the assessee must be the owner of the land on which the housing project is constructed is now settled by the Special Bench in* ***RADHE DEVELOPERS & ORS. VS. ITO & ORS. (2008) 23 SOT 420 (AHD.)*** *In this case, the land was not registered in the Assessee's name. Contention of the Revenue was that in order to claim a deduction u/s. 80IB(10) the assessee must be the owner of the land on which the housing project is constructed. It was held that there was no such condition in the provisions of the Section 80IB(10). Deduction u/s. 80IB(10) is allowable to an undertaking developing and building housing projects, whether it is developed by it as a contractor or as an owner. It was also held that the term "Contractor" is not contradictory to the term "Developer".*

In this case, another important issue before the Bench was whether the profit earned by the assessee included sale of Extra-FSI which was unutilised was eligible for deduction. It was held that there was no condition as it FSI under the Scheme of Sec. 80IB(10). It is not mandatory requirement to fully utilise permissible FSI. In the facts of the case it was held that development agreement with the land owners makes reference to the land area only. Also, the sale deeds executed in the favour of the buyers of the residential houses are for the sale of the plot of the land. In both the documents, the assessee has not acquired or relinquished rights with reference to FSI.

There is no question of selling the unused FSI to the individual buyers or calculating profitability on FSI as the same is not contemplated u/s. 80IB(10). Calculation given in the approved plan is for the maximum permissible FSI. By giving such calculation, it is not mandatory to make construction to the fullest extent of maximum permissible FSI. Therefore, deduction could not be denied to the assessee on the ground that the profit earned by the assessee are not for developing and building housing projects done but for the sale of extra FSI which has not been utilised for developing and building the housing projects.

- *The issue was where an undertaking developing and building housing projects is engaged as a sub-developer and all the sanctions are obtained by the developer whether the sub-developer would be eligible for the deduction or main developer or both. It was held that the sub developer is eligilbe for deduction.*

SAROJ SALES ORGANISATION vs. ITO (2008) 115 TTJ 485.

- *The Tribunal noted that subsequent to the two buildings being constructed on the said plot, the plan of building 'C,' in respect of which the assessee acquired the development right, was approved by the local authority. The original plan was approved in 1995, but final approval was given to the modified plan 10-9-1998 and permission for construction of the building was finally given on 9-10-1998. The Tribunal also noted that in the original approved plan/layout building 'C' was not shown. Having observed that the commencement certificate (CC) was in the name of the original owner since the title of the property was not in the name of the assessee, the Tribunal held that:*

(a) merely because the commencement certificate is issued in the name of the original landowner, the assessee cannot be deprived of deduction u/s.80IB(10) as nowhere it is a mandate of the said provision that the assessee must be the owner of the property which he undertakes to develop;

(b) merely because the agreement is not registered, the assessee cannot be deprived of the deduction u/s.80IB(10) as the assessee has developed building 'C';

(c) merely because the CC was obtained prior to 1-10-1998, that does not mean that the assessee has commenced the development and commencement of the building 'C';

(d) CC was granted for the first time on 24-2-1995 and hence, building 'C' was not part of the original project. It observed that on the said plot the owner had constructed building 'A' consisting of 95 flats and tenements and alsobuilding 'B'. Just because the plot of land remained the same, it cannot be construed that building 'C' is a part of the original housing project;

As regards the objection of the CIT(A) on the area of plot of land on which the project was constructed, the Tribunal on facts found that there was no clearcut finding by the AO and CIT(A) hence it restored the issue to the file of the AO to verify whether the area of the plot on which the building 'C' is constructed is one acre or not. The appeal filed by the assessee was allowed.
Essem Capital Markets Ltd. v. ITO (2011) TIOL 196 ITAT-Mum. [BCAJ]

- *Whether the benefit of extension of the date of completion of project upto 31st March, 2003 were applicable to Asst. Yr. 2001-02 and subsequent years only. In the case it was held that the contention of the Revenue that the amendment on the Section 80IB(10) extending the Date of Completion of the project upto 31st March, 2003 were applicable to the Asst. Yr. 2001-02 and subsequent years and the assessee in the instant case for the Asst. Yr. 2000-01 was not eligible to avail the benefit of the said amendments is not acceptable.*
DY. CIT vs. ANSAL PROPERTIES & INDUSTRIES LTD. (2008) 22 SOT 45 (DEL.)

- *If the plan is approved before 01.10.1998 but the construction of the project starts after 01.10.1998, then the Assessee is eligible to claim deduction u/s. 80IB(10).*

Also, if the plan is approved in the name of Sonal Venture (original owner) but the construction activity was carried out by Shree Ostwal Builders Ltd. (Assessee), then the deduction can be claimed by the Assessee.

Further, Commercial units are entitled for deduction u/s. 80IB(10) if the project is approved before 01.04.2005 as commercial project by the local authority.

Further, ITAT held that if the project is approved as a residential project but later on if any flat purchaser converts the flats into godown then as the builder has no control on the same, the builder is entitled to claim deduction in respect of the same u/s. 80IB(10).

ACIT v. SHREE OSTWAL BUILDERS LTD., I.T.A. No. 2144/MUM/2010.

Points to remember:

- For the removal of doubts, it is hereby declared that nothing contained in this sub-section shall apply to any undertaking which executes the housing project as a works contract awarded by any person (including the Central or State Government).

- Provided that nothing contained in clause (a) or clause (b) shall apply to a housing project carried out in accordance with a scheme framed by the Central Government or a State Government for reconstruction or redevelopment of existing buildings in areas declared to be slum areas under any law for the time being in force and such scheme is notified by the Board in this behalf;

- Proportionate deduction for eligible housing units in a project containing ineligible housing units.

It is held that provisions of sec 80IB(10), do not provide for denial of deduction, if a housing complex contains both the smaller and larger residential units. It concluded that profits attributable to eligible residential units are entitle for deduction inspite of the fact that the other residential units are greater than 1500 sq. ft. build up area.

BENGAL AMBUJA ITA NO./ 1735 (CAL.) 2007

- Deduction in case of individual projects if they are part of bigger project but got sanction separately

It is held that where some of the residential units in a bigger housing project, treated independently, are eligible for relief u/s 80IB(10), relief should be given pro – rata and should not be denied by treating the bigger project as a single unit, moreso, when assessee obtained all sanctions, permissions and certificates for such eligible units separately.

DY. CIT V. BRIGADE ENTERPRISE (P) LTD 119 TTJ 269

- Restriction on commercial area – prospective or retrospective?

It is held that the restrictions on build up area of commercial constructions is effective for projects stated after 1.4.2005. As a result projects stated before 1.4.2005 will not be barred by such imitations.

ARUN EXCELLO FOUNDATION VS. ACIT 108 TTJ 71

In the **High Court of Bombay**, it was held that, *"Direct Taxation Deduction under 80IB(10) of Income Tax Act, 1960 Whether a housing project having commercial area up to 10 per cent of the project is eligible for deduction on the entire profits of the project Under Section 80IB(10) up to 1st April, 2005 Held, Where a project fulfils the criteria for being approved as a housing project, then deduction cannot be denied under Section 80IB(10) merely because the project is approved as residential plus commercial. Section 80IB(10) allows deduction to the entire project approved by the local authority and not to a part of the project. If the conditions set out in Section 80IB(10) are satisfied, then deduction is allowable on the entire project approved by the local authority and there is no question of allowing deduction to a part of the project. In the present case, the commercial user is allowed in accordance with the DC Rules and hence the Assessee was entitled to Section 80IB(10) deduction on the entire project approved by the local authority."*

Ratio Decidendi:"*Where a project fulfils the criteria for being approved as a housing project, then deduction cannot be denied under Section 80IB(10) merely because the project is approved as residential plus commercial and Section 80IB(10) allows deduction to the entire project approved by the local authority and not to a part of the project.*"

CIT-II v. BRAHMA ASSOCIATES (2011) 239 CTR 30, 197 TAXMAN 459 (Bom)

The Assessee, a builder and land developer, had entered into an agreement to develop and construct a building project on land situated at Mira Taluka, Dist. Thane. For A.Y. 2005-06, the Assessee filed a return of income in which it claimed deduction u/s.80IB(10) of the Act. The AO noted that the housing project which consisted of 94,255 sq. ft had shopping area to the extent of 7,935 sq. ft. The AO denied the deduction on the ground that in view of the amendment to section 80IB(10) w.e.f. 1-4-2005, the Assessee was not entitled to deduction u/s.80IB(10) of the Act. Aggrieved the Assessee preferred an appeal to CIT(A) who allowed the appeal. Aggrieved by the order passed by the CIT(A) the Revenue preferred an appeal to the Tribunal.

Held: *The Tribunal noted that the assessee's project had commenced prior to 1-4-2005. It also noted that in the case of Brahma Associates, the High Court has held that the amendment to section 80IB is prospective in operation. Since the assessee's project had commenced in December 2003, the Tribunal held the amendment to be not applicable to the assessee's case.*

The Tribunal dismissed the appeal filed by the Revenue.

ITO v. Chheda Construction Co. (Joint Venture) ITA No. 2764/Mum./2009 [BCAJ]

- One acre area interpretation where eligible and ineligible projects are constructed:

It is held that as per clause (b) to section 80IB(10), the project should be on a size of plot of land which has the maximum area of one acre. As a result eligible projects should be allowed deduction even though ineligible projects are constructed on the same piece of land.

VANDANA PROPERTIES ITA NO. 1253 / MUMBAI / 2007

- A **TERRACE** is known as a paved outdoor area adjoining a residence. It adjoins the residence externally and is not a part of the structure that composes the residential unit. Hence, the terrace area allotted to the flat owners for the exclusive use should not be clubbed with the built up areas of the flats to ascertain whether the maximum built up area of the flat is less than 1000sq.ft. Built up area in order to satisfy the eligibility condition in clause © of Section 80IB (10).

- **COMPLETION OF PROJECTS –** as per the requirement of section 80IB(10), the project is required to be completed by 31.03.2008. For the purpose, whether occupation certificate obtained from the Appropriate Authorities to the effect that the development is as per the approval and is ready for occupation is sufficient or will the department insist on any other certificate like completion certificate from appropriate authorities?

In our opinion, the occupation certificate given by the BMC would be sufficient proof that the housing project is completed. Even in ***DY. CIT vs. ANSAL PROPERTIES & INDUSTRIES LTD. (2008) 22 SOT 45 (DEL.)*** it was considered sufficient. But, occupation certificate are sometimes given building wise. If all the buildings constructed by the developers have occupation certificate before 31.03.08, may be sufficient compliance.

If, by any reason the occupation certificate was not granted or dispute, despite the fact that the project is completed, some other proof like the architect certificate may also help. It is preferable that the certificate should elaborately describe the completed project item wise.

When construction is completed before 31.03.2008, but the sale of some flats take place in subsequent years, deduction u/s 80 – IB (10) can be claimed. Generally, in incentive provisions granting tax holidays, there is always a specification as to the number of years the tax holiday can be enjoyed. But, in Section 80 – IB (10), there is no specification as to the number of years the tax holiday is available.

As on date, it appears that once an approved project is completed before the cut off date fixed as per section 80 – IB (10) and other eligibility conditions are also fulfilled, there is no terminal year for claiming the tax holiday. The assessee will be entitled to deduction u/s 80 – IB (10) in respect of income from the sale, provided that the legislature has not made any amendments curtailing the availability of the deduction upto A.Y. 2009 – 10 or deleted the provisions of the said section with effect from 01.10.2010.

RELIANCE JUTE & IND. LTD. v. CIT(1979)120 ITR 921 (SC).

9. <u>DEVELOPMENT RIGHTS:</u>

DEVELOPMENT RIGHTS – WHO ARE ENTITLE – SOCIETIES OR MEMBERS?

In respect of Tenants co-partnership co-operative societies, which are of the nature of "Flat Owners Societies" in which the flats are acquired by the society from the builder on ownership basis and thereafter Society is formed, and land is conveyed to the society and individual members acquire ownership rights over the building and underneath the development rights.

This concept has been recognized under Bombay stamp Act as on the conveyance in favour of the housing societies, stamp duty paid by the purchasers of flats on ownership agreements is deducted from the stamp duty payable on the market value of the property transferred in favour of the society as per proviso to article 25 of schedule 1 of Bombay Stamp Act.

Circular No. F.N. 4 / 28 / 68 – WT DT. 10.0.1969 AND 27.01.1969 explaining the provisions of section 5(1)(iv), the Board clarify that flats vest with individual members of society and wealth tax exemption will be available to individual members.

I] Additional Area expected at Redevelopment

Liability of Income/Capital Gain Tax, if any, on:-

A. Additional area in the hands of individual members.

Ans. As per Section 54 of the Income Tax Act, 1961, if any residential property which was held for a period of more than 3 years is sold or given for redevelopment and the new flat is purchased or acquired within a period of 1 year before or 2 years after the sale or constructed within 3 years after the sale then capital gain arising on the transfer of the old flat will be exempt to tax u/s. 54 of the Income Tax Act, 1961 to the extent of the cost of such new flat.

In the case of redevelopment, the new flat to be acquired is treated as constructed for the purpose of the Section 54. Thus, if the new flat is acquired by the owner within a period of 3 years from the surrender of the original flat then the capital gain arising from the sale of the original flat can be claimed to be exempted u/s. 54 of the Income Tax Act.

If the new flat is not acquired by the owner within a period of 3years then the Assessing Officer at his discretion can disallow the same at any time during the assessment.

However, allotment of a flat or a house by a cooperative society, of which the assessee is the member, is also treated as construction of the house [Circular No. 672, dated 16-12-1993]. Further, in these cases, the assessee shall be entitled to claim exemption in respect of capital gains even though the construction is not completed within the statutory time limit. [*Sashi Varma* v *CIT* (1997) 224 ITR 106 (MP)]. Delhi High Court has applied the same analogy where the assessee made substantial payment within the prescribed time and thus acquired substantial domain over the property, although the builder failed to hand over the possession within the stipulated period. **[*CIT* v *R.C. Sood* (2000) 108 Taxman 227 (Del)].**

Hence, relying upon the above judgments, even if in the case of development, the new flat is acquired by the owner after a period of 3years from the surrender of the old flat, an assessee can claim exemption u/s. 54.

If the new flat acquired to claim exemption u/s. 54 is sold within a period of three years from the date of purchase then the capital gain exemption claimed earlier would become taxable in the year the new flat is transferred.

Thus, in your case, the Receipt of extra carpet area over and above the existing area could be claimed as exemption u/s. 54 of the Income Tax Act, 1961.

Further, we would like to state that under the definition of "Transfer" according to Sec 2(47) Income Tax Act, 1961, transfer, in relation to a capital asset, includes sale, exchange, or relinquishment of the asset or the extinguishment of any rights therein or the compulsory acquisition thereof under any law.

An exchange involves the transfer of property by one person to another and reciprocally the transfer of property by that other to the first person. There must be a mutual transfer of ownership of one thing for the ownership of another. Hence, the acquisition of new flat would be considered as exchange and would be considered as transfer for the purpose of capital gain.

Argument could not be made that no cost is incurred by any member for the acquisition of the new flat and hence capital gain cannot be computed and the case does not fall within the ambit of Section 55(2). The member is forgoing his rights in the old flat. And hence, it would be considered as the cost of acquisition of the new flat.

However, if the residential flat is held for a period of less than 3 yrs than the receipt of extra area by the individual members would be taxable in the hands of the individual members.

B. <u>Cash compensation received upon surrender of entitled additional area, in part or in full, by an individual member.</u>

Ans. If the Individual member is surrendering a part of the existing area then the Individual member would be liable to pay Capital Gain Tax. The sale consideration would be calculated as per **<u>Section 50C of the Income Tax Act</u>**, which is as follows:
"Where the consideration received or accruing as a result of the transfer by an assessee of a capital asset, being land or building or both, is less than the value adopted or assessed or assessable by any authority of a State Government for the purpose of payment of stamp duty in respect of such transfer, the value so adopted or assessed or assessable shall, for the purposes of section 48, be deemed to be the full value of the consideration received or accruing as a result of such transfer."

However, if the Individual member is surrendering a part of the additional area then the Individual member would not be liable to pay any income tax or capital gain tax on the same.

C. ***The Society for receiving amenities and facilities for the common use of its members and their families.***

Ans. If the Society is receiving for amenities and facilities for the common use of its members and their families then the same is not taxable in the hands of the Society or the Individual members as there is no cost of acquisition of the same.

In deciding the case of ***JETHALAL D.MEHTA V. DY. CIT [(2005) 2 SOT 422 (MUM.),*** Hon. Income Tax Appellate Tribunal mainly relied upon Supreme Court decision in the case of ***CIT V. B.C.SRINVASA SHETTY 128 ITR 294*** in which it was decided that if there is no cost no capital gain can be worked out hence amount received is to be treated as exempt receipt.

II] Corpus Money expected at Redevelopment

Liability of Income/Capital Gain Tax, if any, on:-

A. ***Corpus Money received by the individual members from the Developer in lieu of surrender of part entitlement of FSI/Development rights.***

Ans. If the Individual member is receiving an area which is same or more than the present area then the Individual member is not liable to pay capital gain tax on the same.

If however, Individual member is receiving an area which is less than the present area than the Individual member is liable to pay Capital Gain Tax as per Section 50C of the Income Tax Act, 1961 as already explained above.

B. ***Corpus Money received by the Society from the Developer in lieu of surrender of part entitlement of FSI/Development Rights, such funds being invested by the Society to earn interest income to meet/subsidize the maintenance costs of its Redeveloped premises and property.***

Ans. If at the time of Redevelopment, the Society was in not in possession of unutilized FSI/Development Rights, then the Society would not be liable to pay any Capital Gain Tax on the receipt of the Corpus Money on surrender of a part of FSI/Development Rights.

Further, if the Society has unutilized FSI/Development Rights in its possession at the time of Redevelopment, then the receipt of the Corpus Money on surrender of the part of FSI/Development Rights would be taxable in the hands of the Society.

Also,in the case of (1) ***New Shailaja CHS v. ITO (ITA NO. 512/M/2007. BENCH B dated 2nd Dec, 2008 (mum.)and (2) ITO v. LOTIA COURT CO- OP. HSG. SOC. LTD. (2008) 12 DTR (MUMBAI)(TRIB) 396*** it was held that *where the assessee, a Co-op. Hsg. Soc. Ltd. Became entitled, by the virtue of Development Control Regulations, to Transferable development Rights (TDR) and the same was sold by it for a price to a builder , the question arose whether the transaction of sale receipt could be taxed. It was held that though the TDR was a Capital Asset, there being no 'cost of acquisition' for the same, the consideration could not be taxed.* The same is held in the cases of

NEW SHAILAJA CHS LIMITED (ITA NO. 512/MUM./2007), OM SHANTI CO-OP. HSG. SOC. LTD. (ITA NO.2550/MUM./2008) & **LOTIA COURT CO-OP. HSG. SOC. LTD. (ITA NO. 5096/MUM./2008).**

Further, in the case of **MAHESHWAR PRAKASH 2 CHS LTD. 24 SOT 366 (MUM.)**, it was held that *the assessee-society acquired the right to construct the additional floors by virtue of DCR, 1991 which could not be available to the assessee on expenditure of money. Prior to DCR, 1991, no society had any right to construct the additional floors, so it was not a tradable commodity. Suddenly by virtue of DCR, 1991, the right was conferred by the Government on the assessee. Such right exclusively belonged to the building owned by the society. It could not be transferred to any other building.*

Similarly, similar right belonging to other societies could not be purchased by the assessee for the purpose of constructing additional floors in its own building. Therefore, such right had no inherent quality of being available on expenditure of money and, therefore, cost of such asset could not be envisaged. Hence, the said view was fully justified in terms *of the decision of the Apex Court in the case of B.C. Shrinivasa Shetty.*

Therefore, the right acquired by the assessee did not fall within the ambit of section 45 itself. The amended provisions of section 55(2) were also not applicable, since such right was not covered by any of the assets specified in section 55(2)(a).

Therefore, the sum of Rs. 42 lakhs received by the assessee from the developer was not chargeable to tax under section 45. Therefore, the impugned orders passed by the lower authorities were to be set aside.

C. Corpus Money received by the Society from the Developer (as described in B above) and subsequently distributed to its members. Whether such incomes enlisted above at A, B and C, if taxable, shall be treated as Capital Gains or deemed to be income earned in the year of receipt.

Ans. As per Maharashtra Co-op. Societies Act, 1960, a Co-operative Society cannot distribute the corpus funds to its Individual member, it can only declare dividends. However, the declaring of Dividends has lots of restrictions and formalities.

D. Liability of Income Tax, if any, on interest income arising from investment of such Corpus Money by the Society/individual members in the Co-operative/other Banks.

Ans. If the Society receives interest income form a Co-operative bank then the same is exempt from tax. And, if the interest income is received from other banks than the same is taxable and the Society has to pay tax on the same.

However, as per recent Hon'ble **Tribunal Judgment** in the case of **ITO v. Sagar Sanjog C.H.S. Ltd., ITA Nos. 1972 to 1974 and 2231 to 2233/ Mum./ 2005(BCAJ)** it was held that *the interest income earned out of the fund money invested went to reduce the maintenance. According to the tribunal, the interest would* *have been taxable, had there been surplus left after it being adjusted against the maintenance expenses. The tribunal also noted that there was nothing on record to suggest that the interest income would be given to members on dissolution of the Society.*

Thus, even the interest income received from other than Co-operative Bank and spent on Society's work then the concept of Mutuality will apply and is not liable to tax but this view is not free from litigation.

III] Rent for Temporary Alternative Accommodation including Deposits, if any:

Rental allowance may be received by individual members in the event of need for Relocation during Redevelopment. Such amounts may be utilized in part or in full towards rent paid for alternative premises or may remain entirely unspent if the member already has his/her own alternative accommodation. Such allowance may be received for about three years, either together in one tranche in advance or in installments on a staggered basis.

Liability of Income Tax, if any, on such Rental Allowance, including Deposits, if any, received by the individual members.

A. Whether such income, if taxable, shall be treated as income earned in the year of receipt (if received on a staggered basis) or entirely as income in one year (if received fully in advance)

Ans. In order to get the old building redeveloped, the existing structure of the old building is required to be demolished and hence, it is necessary to vacant the same. To facilitate redevelopment and to compensate the flat owners for the hardship to be faced by them in this regard, the Developer might offer them Rent compensation which they would be paying for the temporary accommodation during the period of redevelopment.

The Rent Compensation so provided by the developer to the owner should be expended by the owners for the purpose of their temporary accommodation and other expenditure related thereto.

If the actual rent paid by the flat owners is less than the Rent compensation received by them from the redeveloper then the excess of such amount received will be taxable under the head **Income from Other Sources,** otherwise, the Rent compensation received by the flat owners from the redeveloper is not taxable.

The Rent Compensation given to the Individual Members shall be taxable in the year of receipt if the Rent Compensation is received on staggered basis and the whole is not spend by the Individual Members on their alternative accommodation.

However, if the Rent Compensation is given to the Individual Members in one tranche in advance, then the Rent Compensation received by the Individual Members would be taxable on proportionate basis if the same is not spend on the Alternative Accommodation.

IV] Hardship Allowance/ Compensation for Inconvenience.

Members opting not to be temporarily relocated during the Redevelopment may receive "Hardship Allowance" from the Developer.

Members agreeing to be temporarily relocated during Redevelopment may receive "Compensation for Inconvenience" from the Developer.

A. Liability of Income Tax, if any, on such Allowance/ Compensation and if taxable, mode of computation i.e. whether as income in the year of receipt or whether on a staggered basis as received.

Ans. Along with extra area and Rent compensation, the redevelopers also offer lumpsum amount to the flat owners in addition to extra area and compensation. The transfer of TDR to Builder for development of property does not attract Capital Gain Tax.

In deciding the case of ***JETHALAL D.MEHTA V. DY. CIT [(2005) 2 SOT 422 (MUM.),*** Hon. Income Tax Appellate Tribunal mainly relied upon Supreme Court decision in the case of ***CIT V. B.C.SRINVASA SHETTY 128 ITR 294*** in which it was decided that if there is no cost no capital gain can be worked out hence amount received is to be treated as exempt receipt.

Hence, the Hardship Allowance and the Compensation for Inconvenience is not taxable in the Hands of the Individual Members as Hardship Allowance and Compensation for Inconvenience can't be worked out in monetary terms and have no cost. Since there is no cost of acquisition, as per Income Tax Act, 1961, the receipt would not be treated as a Capital Receipt and thus, is exempt from tax.

V] Goods/ Household Amenities received by Members from Developer.

A. Liability of Income Tax, if any, on individual members for any property other than immovable property that are sometimes included by Developers in the new premises on a complimentary basis.

Ans. Property other than immovable property which are not attached to the walls of the flat and exceeds 50,000/- in value in totality are not treated as a part of the Flat and are thus taxable in the hands of the Individual Members in the year of receipt of such amenities u/s. **56(2)(vii) of the Income Tax Act, 1961**, if property is covered under section, which is as follows:

"where an individual or a Hindu undivided family receives, in any previous year, from any person or persons on or after the 1st day of October, 2009,--

(a) any sum of money, without consideration, the aggregate value of which exceeds fifty thousand rupees, the whole of the aggregate value of such sum;

(b) any immoveable property,-

(i) without consideration, the stamp duty value of which exceeds fifty thousand rupees, the stamp duty value of such property;

(ii) for a consideration which is less than the stamp duty value of the property by an amount exceeding fifty thousand, the stamp duty value of such property as exceeds such consideration:

Provided that where the date of the agreement fixing the amount of consideration for the transfer of immoveable property and the date of registration are not the same, the stamp duty value on the date of agreement may be taken for the purposes of this sub-clause:

Provided further that the said proviso shall apply only in a case where the amount of consideration referred t therein, or part thereof, has been paid by any mode other than cash on or before the date of agreement for the transfer of such immoveable property;

(c) any property, other than immovable property,--

(i) without consideration, the aggregate fair market value of which exceeds fifty thousand rupees, the whole of the aggregate fair market value of such property;

(ii) for a consideration which is less than the aggregate fair market value of the property by an amount exceeding fifty thousand rupees, the aggregate fair market value of such property as exceeds such consideration"

"property" means the following capital asset of the assessee, namely:-

- *Immovable property being land or building or both*
- *Shares and securities*
- *Jewellery*
- *Archaeological collections*
- *Drawings*
- *Paintings*
- *Sculptures*
- *Any work of art*
- *bullion*

The provisions of section 56(2) (vii) are amended, with effect from 01.04.2014, so as to provide that where any immoveable property is received by an individual or HUF for a consideration which is less than the stamp duty value of the property by an amount exceeding Rs.50,000, the stamp duty value of such property as exceeds such consideration, shall be chargeable to tax in the hands of the individual or HUF as income from other sources.

In other words, if the difference between stamp duty value and the purchase consideration is Rs.50,000 or less, nothing will be chargeable to tax in the hands of the recipient of property. If the purchase consideration is less than the stamp duty value of the property and such difference is more than Rs.50,000, then the difference between the stamp duty value and purchase consideration will be taxable under section 56 under the head 'Income from Other Sources'.

The following are important points to be noted:

(A) The immoveable property received should be land or building or both.

(B) The immoveable property is received during the previous year.

(C) The immoveable property is received on or after 01.04.2013

(D) The immoveable property received may be situated anywhere [whether in India or abroad].

(E) The immoveable property should be a capital asset as defined under section 2(14).

(F) The immoveable property so received should be for a consideration less than the stamp duty value and the difference between the two should exceed Rs.50,000. In such a situation, difference between the stamp duty value and purchase consideration will be taxable.

(G) Rs.50,000 limit for difference to be applied property wise, i.e. specially to each property received for consideration less than stamp duty value and not to all such properties received during the previous year.

(H) It would appear that the provisions would apply only if consideration is quantifiable in money terms. If not, it would appear that the provisions would not apply.

VI] Reimbursement of Expenses from Developer.

A. ***Liability of Income Tax, if any, on the Society/ individual members for Reimbursement from Developer of Expenses such as Stamp Duty, Fees of Consultants (Architect, Lawyers, Chartered Accountants, etc.) cost of updating members and holding General Body meetings, Administrative Expenses towards the Redevelopment Process, etc. incurred/ to be incurred.***

Ans. Anything amount which is reimbursed by the Developer is not taxable either in the hands of the Society or the Individual Members, provided that the entire amount of reimbursement is been spent on the expenses it is reimbursed for.

Thus, if excess amount is reimbursed by the Developer than the amount which is actually spent for the purpose than the excess amount would be taxable on the receipt of the same.

However, in the case of a Society, if excess amount is reimbursed to a Society by the Developer than actually spent by the Society, and the excess amount so received is been used by the Society for payment of expenses which are for the welfare of the Society or the Individual Members than the excess amount received by the Society would not be taxed and hence, would be exempt. Otherwise the excess amount received by the Society would be taxable.

VII] Liquidation & Disbursement of Existing Sinking Fund.

A. ***Liability of Income/Capital Gain Tax, if any, on the Society/ individual members upon liquidation and disbursement to existing members (with permission from Registrar/any other authority) of existing, unutilized Sinking Fund (generated by annual contributions from members and bank interest earned thereon.) prior to induction of new members arising from saleable portion of Redeveloped premises.***

Ans. In our view, the Sinking Fund is to be used on the property itself either for the purpose of development or Heavy Repair.

However, if the Registrar gives permission then the Sinking Fund could be distributed amongst the Individual Members which again has a number of restrictions.

This distribution of Sinking Fund after the permission of the Registrar would be taxable in the hands of the Individual Members to the extent of the interest on such a fund. The distribution of the principal amount would not be taxable in the hands of the Society or the Individual Members.

VIII] TDS on receipt.

A. Whether tax shall be deducted at Source (TDS) from Corpus Money, Allowances, Compensations, Reimbursement of Fees of Consultants and other Expenses, Rent for Temporary Alternative Accommodation and Deposits or any other form of receipt in the hands of the Society/ its individual members.

Ans. As per the Income Tax Act, 1961, no TDS is to be deducted on the amount reimbursed by the Developer to the Society or the Individual Members or on other items such as Corpus Money, Allowances, Compensations, Reimbursement of Fees of Consultants and other Expenses, Rent for Temporary Alternative Accommodation and Deposits or any other form of receipt.

However, when the Society makes payments such as Professional Fees, Contractor, etc, the Society is to Deduct Tax at Source at the rate given herebelow and pay the same to the Income Tax Department and file the Quarterly Returns:

Contractor	1% in the case of individual/HUF
	2% in the case of others u/s 194C
Rent	10% u/s 194I
Professional Fees	10% u/s 194J
Commission & Brokerage	10% u/s 194H

IX] Tax Planning (Saving) Instrument.

A. Recommendation of umbrella of designated schemes, funds, securities, etc. under which the Society/ its individual members may invest taxable proceeds, if any, to minimize the impact of Income/ Capital Gain Tax.

Ans. In our view, whether there would be any capital gain tax liability arising on account of such transactions of Redevelopment, is not free from litigation, in view of the fact that various litigations are going on in various courts in our country and the issue would finally be settled when the Supreme Court decides the matter.

It is also to be noted that even the Supreme Court changes its view from time to time depending on the frequent amendments in the Income Tax Laws.

Further we would like to state that Income Tax Department have filed appeal before Hon. High Court and, if the court allows them against the assessee then the same would be taxable for the Society otherwise till now it is tax free. Even assuming that Hon High Court decide the case against the assessee then assessee will be liable to pay tax with interest but no penalty can be charged in view of recent decision of Supreme Court decided in the case of ***Reliance Petro products Pvt. Ltd. Vs. CIT 92010) 322 ITR 158 (SC)*** on the principle that if assessee give all particulars of income in return and claim certain wrong deduction due to ignorance of highly technical law then that will not attract penalty u/s 271(1)(c) of the Income Tax Act, 1961.

Further we would like to say that based on the above, till now the Corpus received by the Society and the individual members is tax free but in case the High Court decides the case against the Society then to be on the safer side and to avoid litigation with the Income Tax Department, we suggest that recipient can invest the same in Specified Bonds to claim exemption u/s. 54EC of the Income Tax Act. One can earn interest by investment in the Bonds for 3 yrs which would be an added benefit. The interest so earned would be taxable. Section54EC of the Income Tax Act, 1961, is produced here below:

"Where the capital gain arises from the transfer of a long-term capital asset and the assessee has, at any time within a period of six months after the date of such transfer, invested the whole or any part of capital gains in the long-term specified asset, the capital gain shall be dealt with in accordance with the following provisions of this section,

- *if the cost of the long-term specified asset is not less than the capital gain arising from the transfer of the original asset, the whole of such capital gain shall not be charged under* section 45 *;*
- *if the cost of the long-term specified asset is less than the capital gain arising from the transfer of the original asset, so much of the capital gain as bears to the whole of the capital gain the same proportion as the cost of acquisition of the long-term specified asset bears to the whole of the capital gain, shall not be charged under* section 45*:*

Provided that the investment made on or after the 1st day of April, 2007 in the long-term specified asset by an assessee during any financial year does not exceed fifty lakh rupees.

"long-term specified asset" for making any investment under this section during the period commencing from the 1st day of April, 2006 and ending with the 31st day of March, 2007, means any bond, redeemable after three years and issued on or after the 1st day of April, 2006, but on or before the 31st day of March, 2007, -

a) by the National Highways Authority of India constituted under section 3 *of the National Highways Authority of India Act, 1988 (68 of 1988); or*

b) by the Rural Electrification Corporation Limited, a company formed and registered under the Companies Act, 1956 (1 of 1956),

and notified by the Central Government in the Official Gazette for the purposes of this section with such conditions (including the condition for providing a limit on the amount of investment by an assessee in such bond) as it thinks fit

X] Implications of VAT/Service Tax.

A. Whether all receipts in the hands of the Society/ its individual members shall be net of Vat and Service Tax Responsibility/ liability of Society/Its Members towards the same for services rendered to it by professionals/consultants.

Ans. As Society is not providing any Services to the Developer, the Society is not liable to pay Service Tax or VAT on any of the payments receipt by the Society in the form of reimbursements or Corpus Money or Compensations, etc.

If the Society is making any payment of Fees to the Professionals or Contractors, then the Society is liable to pay Service Tax @10.3% to the Professionals and Service Tax or Vat to Contractors on such a payment.

The professionals and the Contractors would in turn pay the same to the respective Central Government or State Government as applicable.

XI] Responsibility/ Liability towards stamp duty.

A. Responsibility/Liability of the Society/its individual members towards Stamp Duty, if any, in transition from surrender of existing premises to the Develop to the occupation and registration of the Redeveloped premises

Ans. Normally, in the cases of Redevelopment, the Stamp Duty and the Registration Charges on surrender of the existing premises to the Developer for the purpose of Redevelopment would be paid by the Developer.

Whereas, when the Individual Members receives the Redeveloped Premises from the Developer, he is liable to pay Stamp Duty and Registration Charges on the same. The Stamp Duty payable would be on the cost of construction of the present area of the Premises and on the market value for the extra area received as per the Ready Reckoner Value published by the Government of Maharashtra every year on 1st January.

XII] Restructuring of Society.

A. Whether the composition of the Society may need to be restructured in any manner so as to facilitate minimization of the tax liability.

B. Whether admission of new members (from saleable portion.) in the existing Society or their Accommodation as an independent new Society would have any bearing on the tax liability of the Society/its individual members.

Ans. No, the composition of the Society need not be restructured in any manner so as to facilitate minimization of the tax liability.

The admission of the new members to the existing Society or their accommodation to the new Society would not make much difference to the tax liability of the Society or its Individual Members.

However, it would be advisable to admit the new members to the existing Society because due to increase in the number of the Members of the Society, the fixed charges or expenses of the Society like maintenance, etc would be distributed amongst the Members.

10. TAX AUDIT

Amount received as advance by builder following project completion method whether tax audit applicable and penalty under section 271B imposable

In case it is taken that assessee is following the system in which income is returned on completion of the project and in case project goes on for more than 5 years and assessee gets its books of account audited for last year in which project is completed, then from where A.O. will be able to verify the figures of expenses and receipts etc. of earlier years. So, it is against the very principle of Section 44AB that in project completion assessee would get the books of account audited in the last year and not in earlier years when he is debiting the expenses and showing sundry debits and different types of receipts are also there. On the basis of above, it can be concluded that audit is to be carried on for all the assessment years during which the project was constructed and the expenses were debited to the P & L A/c.

It is held that amounts received as advance by the assessee-builder from customers had an element of profit and same were to be adjusted towards the cost of flats booked by each customer and thus, the amounts of advance have to be included in "gross receipts" for the purpose of s. 44AB; assessee being under obligation to get its accounts audited under s. 44AB. It cannot be contended that the assessee following project completion method would get the books of account audited in the last year and not in earlier years when he is debiting the expenses and other items and showing different types of receipts penalty under s. 271B was imposable for its failure to get the same done

Gopal krishan Builders [2006] 92 TTJ 215 (Luck)]

11. CAPITAL GAIN

11.1 CAPITAL ASSET

Definition of Capital asset is given under section 2(14) which is very vide in nature and covered the right in capital asset also. Only those item are not covered under capital asset which are specifically excluded from capital asset.

Some Recent Amendment with respect to Definition of capital asset.
By the provision of “Sec. 2(14) Capital Asset”, Rural agriculture land was exempt from capital gain. For being rural agriculture land, land must be satisfied certain condition laid down in section 2(14).The Finance Minister amended this conditions through Finance Bill 2013-14. For, Simplicity we discuss effect of this amended in two part.

A. Criteria for being rural agriculture prior to 01/04/2013
B. Criteria for being rural agriculture after to 01/04/2013

Criteria for being rural agriculture prior 1-04-2013:
Prior to 01/04/2013 this section are applicable:
2(14)(iii) [Agricultural land in India, not being land situate-

(a) in any area which is comprised within the jurisdiction of a municipality (whether known as a municipality, municipal corporation, notified area committee, town area committee, town committee, or by any other name) or a cantonment board and which has a population of not less than ten thousand according to the last preceding census of which the relevant figures have been published before the first day of the previous year; or

(b) in any area **within such distance**, not being more than eight kilometers, from the local limits of any municipality or cantonment board referred to in item (a), as the Central Government may, having regard to the extent of, and scope for, urbanization of that area and other relevant considerations, specify in this behalf by notification in the Official Gazette;]

Thus, if these conditions are satisfied than land will agriculture land.

Land is situated in any within the jurisdiction of a municipality or a cantonment board having population of less than 10000.

Land is situated outside the notified distance from jurisdiction of municipality. Govt. can notified maximum distance of 8Km.

If this condition was satisfied than land is rural agriculture land. And not liable for capital gain tax.

How to measure distance was not given in the definition. Therefore it was taken by road. And same view was followed in following judicial pronouncement.

(1) CIT V.LAL SINGH [2010] 195 TAXMAN 420 (PUNJ. & HAR.)

(2) CIT V. SANTINDER PAL SINGH [2010] 188 TAXMAN 54 (PUNJ. & HAR.)

(3) LAUKIK DEVELOPERS V. DY .CIT [2007] 105 ITD 657 (MUMBAI)

Criteria for being rural agriculture After 1-04-2013:

After 01/04/2013 this section are applies as follow:

As Per Section 2(14)" capital asset" means property of any kind held by an assessee, whether or not connected with his business or profession, but does not include-

(iii) Agricultural land in India, not being a land situated

- In any area which is comprised within the jurisdiction of a municipality (whether known as municipality, municipal corporation, notified area committee, town area committee, town committee, or by any other name) or a cantonment board and which has a population of not less than ten thousand [according to the last preceding census of which the relevant figures have been published before the first day of the previous year]; or

b) In any area within the distance, ***measured aerially,***-

(I) Not being more than two kilometers, from the local limits of any municipality or cantonment board referred to in item (a) and which has a population of more than ten thousand but not exceeding one lakh; or

(II) Not being more than six kilometers, from the local limits of any municipality or cantonment board referred to in item (a) and which has a population of more than one lakh but not exceeding ten lakh; or

(III) Not being more than eight kilometers, from the local limits of any municipality or cantonment board referred to in item (a) and which has a population of more than ten lakh.

Explanation.—*For the purposes of this sub-clause, "population" means the population according to the last preceding census of which the relevant figures have been published before the first day of the previous year;*

Thus, if this condition is satisfied then agriculture land will be rural agriculture and accordingly not liable for capital gain tax.

Land is situated in any within the jurisdiction of a municipality or a cantonment board having population of less than 10000.

Distance of land from municipality and population limit.

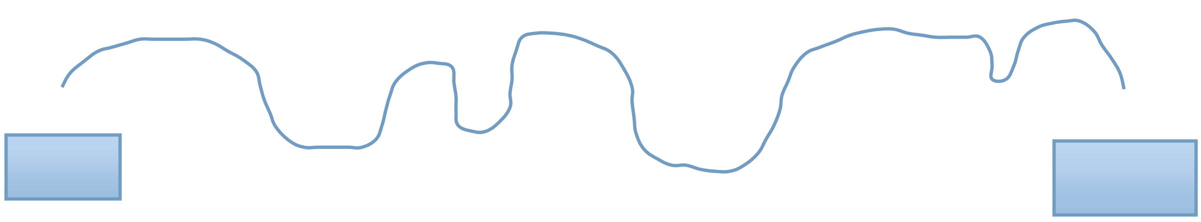
Distance	***Population***
Within 2 kilometers	*10,000-1,00,000*
2 kilometers – 6 kilometers	*1,00,000-10,00,000*
6 kilometers – 8 kilometers	*More than 10,00,000*

The distance from the Municipal Corporation measurement:

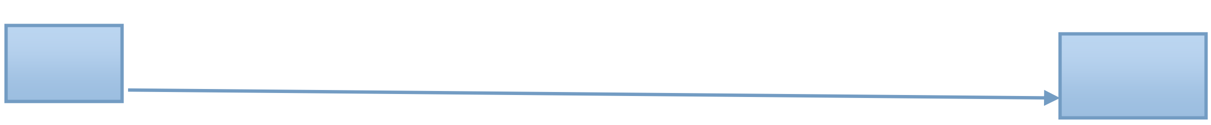
Such distance is to be measured on **straight line aerially** as crow flies. The shortest aerial distance has to be considered. Such shortest aerial distance is defined as "A straight line distance between two places." A human would travel further to get from one point to another due to obstacles or lack of roads or trails, but a crow can go in a straight line between them. Humans have to follow roads which have their twists and turns. But, a crow does not have to face the barriers that humans face. Hence, we measure the straight line distance between two places.

"The distance as the crow flies is a way to describe the distance between two locations without considering all the variable factors. As an example, traveling from California to maine involves a rather indirect route around, over and through mountain ranges and so forth. The driving distance might be about 3,500 miles, but the distance as the crow flies is about 2,800 miles.

Human [By road]



Crow's flight straight line distance (aerial measurement)



This amendment apply in relation to assessment year 2014-15 and subsequent assessment years.

Effect of the amendment

a) Distance from jurisdiction or municipality or cantonment board within which agricultural land is to be considered as urban land has been changed from uniformly 8 kms to within 8 kms depending on population of municipality or cantonment board.

b) Distance to be measured straight line aerially as crow flies and not by road method which was used by courts in various decision. This amendment overcomes above court decisions which say that distance should be measured by road.

c) More land will be covered under the urban land because aerially distance covered more area.

d) Earlier only notified area were covered under the distance criteria but from now any area will be covered under the distance criteria.

11.2 TRANSFER IS A PRE-REQUISITE FOR TAXING CAPITAL GAIN BECAUSE CAPITAL GAIN IS CHARGEABLE IN THE YEAR WHEN ASSET IS TRANSFER:

Capital gain arises only when there is a *transfer* of capital asset. If the capital asset is not transferred or if there is any transaction which is not regarded as transfer, there will not be any capital gain. However w.e.f. assessment year 2000-2001 section 45(1A) has been inserted to provide that in case of profits or gains from insurance claim due to damage or destruction of property, there will be capital gain on such deemed transfer although no asset has been actually transferred in such case.

- **Judicial pronouncements — whether a transaction constitutes transfer or not?**

Where an assessee gives up the right to claim specific performance for purchase of immovable property it is relinquishment of a capital asset and thus transfer:

The assessee had entered into an agreement to purchase certain property. Both parties reserved the right to specific performance of the agreement. Nearly four years thereafter, again another agreement was entered into in the nature of deed of cancellation, by which the assessee agreed for termination of the earlier agreement and allowed the owner of the land to sell the said property to any person and at any price of his choice. As a consideration for this, the assessee was paid a sum of Rs. 6,00,000 apart from being refunded the advance of Rs. 40,000. The question that arose for consideration was as to whether the amount of Rs. 6,00,000 received by the assessee from the vendor could be treated as capital gains in the hands of the assessee.
K.R. Srinath v Asstt. CIT (2004) 268 ITR 436 (Mad)

There is no transfer in family settlement:

Where a family settlement/ arrangement is arrived at in order to avoid continuous friction and to maintain peace among the family members, the family arrangement is governed by the principles which are not applicable to dealing between strangers. So, such *bona fide* realignment of interest, by way of effecting family arrangements among the family members would not amount to transfer. ***CIT v A.L. Ramanathan (2000) 245 ITR 494 (Mad)*** In this case the court followed the decision of the Supreme Court in general law laid down in the case of ***Kale v Deputy Director of Consolidation (1976) AIR 1976 SC 807.***

Giving up the right to obtain conveyance of immovable property amounts to transfer of a capital asset:

Where the assessee had paid the earnest money and acquired right to obtain conveyance of immovable property, such earnest money paid shall be cost of acquisition of such right and if such right is given up, there is a transfer of a capital asset and the compensation received for giving up such right is the consideration price. ***CIT* v *Vijay Flexible Container*** **(1990) 186 ITR 693 (Bom)**

In case of litigation pending, no capital gain tax unless the case is decided:

The AO hold that the income accrues on the date when an enforceable debt is created in favour of the Assessee. However, the Court held to consider the issue as to whether the income would accrue even when the very existence of the income is under doubt and a subject matter of litigation. Further, the subject matter of litigation cannot be a subject matter of tax avoidance.

ITO v. M/s. S. P. BUILDERS, CIT(A) XII/ 12(3)(4)/ IT – 184/07-08.

- ***RECENT AMENDMENTS IN THE FINANCE (NO.2) ACT, 2014:***

In relation to compulsory acquisition of a capital asset, any enhanced compensation received pursuant to an interim order of any authority, will be liable to tax in the previous year in which the final order of such authority is made and not on receipt.

11.3 CONVERSION OF CAPITAL ASSET INTO STOCK – IN – TRADE

As per section 45(2) if a capital asset is converted into stock – in – trade, the capital gain is taxable in the year such stock sold, and the fair market value of the asset on the date of such conversion or treatment shall be deemed to be the full value of consideration received or accruing as a result of the transfer.

11.4 CONVERSION OF STOCK – IN – TRADE INTO CAPITAL ASSET

It was held that there is no provision similar to section 45(2) with respect to Conversion of Stock – In – Trade into Capital Asset. It was further held that holding period is to consider from the date of acquisition.

CIT V. BRIGH**T STAR INVESTMENTS (P) LTD (2008) 24 SOT 288 (BOM.)**

KALYANI EXPORTS & INV (P) LTD & ORS. V. DY. CIT (2001) 78 ITD 95 (PUNE) (TM) (139 AND 140)

However in ***SPLENDOR CONSTRUCTIONS (P) LTD VS. ITO (2009) 27 SOT 39 (DELHI).***

It was held that the period to be considered from the date of conversion to investment. This decision has not considered the decision of the Mumbai Tribunal in Bright Star (supra).

11.5 PIECEMEAL TRANSFER

In **AJAI KUMAR SHAH JAGATI V ITO (1995) 55 ITD 348 (DEL.) AND M/S G. G. DANDEKAR MACHINES WORKS LTD V. JCT, ITA NO. 181/MUM/2001, BENCH – F, DATED 28TH FEBRUARY,2007,** possession of only a part of property was transferred against proportionate consideration received during the relevant assessment year. It was held that capital gains arising only on the said proportion amount of consideration could be charged in the relevant year and not on the entire consideration stipulated in the sale agreement.

11.6 CAPITAL ASSETS CAN EITHER BE SHORT-TERM CAPITAL ASSET OR LONG-TERM CAPITAL ASSET

- **Short-term capital asset:** A capital asset held by an assessee for not more than 36 months *immediately preceding the date of its transfer* is known as a short term capital asset.
- **Long-term capital asset:** It means a capital asset which is not a short-term capital asset. In other words, if the asset is held by the assessee for more than 36 months or 12 months, as the case may be, such an asset will be treated as a long-term capital asset.

- ***RECENT AMENDMENTS IN FINANCE (NO.2) ACT, 2014:***

  Time limit of qualifying as a long term capital asset in case of unlisted share and units of mutual funds (other than equity oriented funds) is now increased from 12 months to 36 months.

Thus, period of holding of a capital asset is relevant for determining whether capital asset is short-term or long-term.

Exclusion/inclusion of certain period for computing the period of holding of an asset:

Case	*Exclusion/Inclusion of period*
(*ii*) Property acquired in any mode given under section 49(1) (*e.g.* by way of gift will, etc.)	Include the holding period of previous owner also.

Judicial decisions for determining period of holding

Property constructed on a land purchased earlier: In case of property is constructed on a site purchased much earlier, the question arises whether the period of holding the asset *i.e.*, the property, should be reckoned from the date of completion of the construction of the property or from the date of acquisition of the land.

The correct position is that the asset consists of two components: (1) Land and (2) Building. When the property is sold, the period of holding has to be reckoned separately for the land and the building. The consideration received can also be split into two parts relating to each component.

*In **CIT v Vimal Chand Golecha (1993) 201 ITR 442 (Raj)**, the land was* *purchased in 1962 and building was constructed thereon in the accounting years relevant to assessment years 1968-69, 1969-70 and 1970-71. The building was sold in 1970. It was held that the gains attributable to land were assessable as long-term capital gains. The gains attributed to the building were however, short-term capital gains. Similar decision was held in the cases of* ***CIT v Lakshmi B. Menon (2003) 264 ITR 76 (Ker) and CIT v C.R. Subramanian (2000) 242 ITR 342 (Kar)****.*

Agreeing with the above Rajasthan High Court view, it has been held that land can be considered a separate capital asset even if a building is constructed thereon. Thus, where the land is held for more than a prescribed period, the gains arising from the sale of the land can be considered as long-term capital gains even though the building thereon, being a new construction, is held for a period less than the prescribed one .

CIT v Dr. D.L. Ramachandra Rao (1999) 236 ITR 51 (Mad)
CIT v Citibank N.A. (2004) 260 ITR 570 (Bom)
In the above cases, the burden will be on the assessee to satisfy how much of the sale proceeds should be apportioned for the land and how much of the sale proceeds pertained to the structure.
CIT v Estate of Omprakash Jhunjhunwala (2002) 254 ITR 152 (Cal)

<u>Period of holding of share in the co-operative housing society:</u> While computing the capital gain tax in case of transfer of his shares by a person who is a member of cooperative housing society, the relevant date would be date on which the member acquires the shares in the cooperative housing society and the date on which member had sold his shares therein. Thus, where the assessee acquired shares in the society on 6-9-1979 and was allotted flat on 15-11-1979. He was given possession of flat in October 1981, and sold the shares of the society along with the flat, on 4-12-1982, the capital gains arising from the sale were long term capital gains, shares having been held for more than 36 months.
CIT v Anilben Upendra Shah (2003) 262 ITR 657 (Guj)

Similarly, the assessee became a member in Venus Apartments (Galaxy Co-operative Housing Society). He was allotted a flat in the building of the society by resolution dated 4-11-1980, passed by the managing committee of the society. On the date of allotment, i.e., 4-11-1980, the property was under construction and came to be completed on 12-9-1983. Physical possession was handed over to the assessee on 12-9-1983. On 30-4-1984, the flat was sold by the assessee for a consideration of Rs. 3,75,000. The assessee worked out long-term capital gains at Rs. 1,59,395. The Assessing Officer did not accept the stand of the assessee that the assessee had become the owner of the property as per resolution dated 4-11-1980.

According to the Assessing Officer the assessee had held the property for a period of less than 36 months and as such was liable to short-term capital gains tax, it was held that the assessee in the present case was allotted a share by the co-operative housing society on 4-11-1980, and the sale of the same took place on 30-4-1984, i.e., after a period of 36 months. The Tribunal was therefore justified in holding that the capital gains arising were *long-term capital gains and the assessee was entitled to deduction from such gains as per law.*

CIT v Jindas Panchand Gandhi (2005) 279 ITR 552 (Guj)

<u>*Right to acquire any house property*</u>: Where a flat is booked with a builder under a letter of allotment or an agreement for sale, this would represent only a right to acquire a flat and if such right is acquired more than 36 months back, it becomes a long-term asset. However, when the possession of the flat is taken, the period of holding would once again commence from the date of the possession of the flat as the small right to acquire a flat merged into larger right and small right upon a merger would loose its existence.

11.7 COST OF ACQUISITION

Cost of acquisition of an asset is the value for which it was acquired by the assessee. Expenses of capital nature for completing or acquiring the title of the property are includable in the cost of acquisition.

<u>*Judicial decision on cost of acquisition:*</u>

Cost of acquisition of an asset acquired from the previous owner in any mode given u/s 49(1): In this case, the cost of acquisition is taken as the cost to the previous owner and it is this cost which will have to be indexed. For the purpose of indexation the year in which the asset was *first held* by the assessee (not the previous owner) is to be considered. The indexation will be done as under:

$$\text{Cost of acquisition to the previous owner} \times \frac{\text{CII of the year of transfer}}{\text{CII of the year in which the asset is first held by the assessee}}$$

However, in the case of *Mrs**. Pushpa Sofat*** **(2002) 81 ITD 1 (Chd)(SMC),** the indexation of cost was allowed from the date of acquisition of the asset by the previous owner and not the date when the asset was acquired by the assessee from the previous owner under any mode given under section 49(1).

Now, the Hon'ble Bombay High Court also take a same view in case of ***CIT V/S Manjula J. Shah [2012]204TAXMAN691(Bom HC)*** *that* under any mode given under section 49(1) i*ndexation will be allowed from the date when previous owner acquired property.*

11.8 VALUATION AS ON 1.4.1981

Reference to the DVO can be made u/s 55A only when the AO is of the opinion that the value of the capital asset claimed by the assessee is less than the fair market value and not when he was of the opinion that the fair market value of the property as on 01.04.1981 as shown by the assessee was more than its actual fair market value.

Cit V. Daulat Mohta Huf Ita No. 1031 Of 2008 Dt. 22.09.2008 (Bombay High Court)

Ito V. Smt. Lalitaben B. Kapadia (2008) 115 Ttj 938 (Mum.)

Patel India (P) Ltd. V. Dy. Cit (1999) 63 Ttj 19 (Mum.)

However the word *"less than the fair market value"* is substituted with the word "*at variance"* by Finance Act 2012, w.e.f. 01.07.2012. Therefore w.e.f. 01.07.2012 reference to the DVO can be made u/s 55A when the AO is of the opinion that the value of the capital asset claimed by the assessee is at variance with its fair market value.

Therefore, **after 1st July 2012** assessing officer has power to refer matter to DVO if the assessing officer is of opinion that the value so claimed is more than the fair market value than Department can challenged 1981 valuation valued by registered valuer and refer the valuation of asset to the valuation officer.

11.9 FORFEITURE OF ADVANCE AGAINST CAPITAL ASSET

Earlier by virtue of section 51 forfeiture of advance received for transfer of capital asset was reduced from the cost of acquisition which result into loss to tax payer at the time of sale of capital asset. Because on sale of capital asset he loos the indexed benefit if the advance was not forfeited. Therefore, to avoid this loophole new section 56(2)(ix) was introduced **vide Finance (No.2) Act, 2014** and as per new section cost will remain same and advance will be taxed under "Income from other source".

Ex.:- Cost of asset as on 1.4.1981 RS. 1,00,000/-, Advance forfeited in A.Y. 2014-15 Rs. 50,000/-, Index of A.Y. 1981 = 100, Index of A.Y. 2014 = 1024, Final Sale for = Rs. 15,00,000/-, Sale in A.Y. 2014-15

Earlier Provision		***Proposed Provision***	
Income From Capital Gain		**Income From Capital Gain**	
Sale	Rs. 15,00,000/-	Sale	Rs. 15,00,000/-
Less: Index Cost (1,00,000 – 50,000)*1024/100	Rs. 5,12,000/-	Less: Index Cost 1,00,000*1024/100	Rs. 10,24,000/-
Long Term Capital Gain	**Rs. 9,88,000/-**	**Long Term Capital Gain**	**Rs. 4,76,000/-**
		Other Source Income	
		Forfeiture of Advance	Rs. 50,000/-
Total Income	**Rs. 9,88,000/-**	**Total Income**	**Rs. 5,26,000/-**

11.10 EXEMPTION OF CAPITAL GAINS U/s. 54, 54B, 54EC & 54F

a) *Profit on transfer of house property used for residence [Section 54]*:

Benefit of section 54 is confined to sale of a residential house after 36 months and reinvestment in a residential house. Reinvestment benefits are available both for purchase and construction of the house. Purchase has to be either one year before or two years later. Construction has to be completed within three years of the sale of the asset in respect of which benefit of reinvestment is claimed. There have been many decisions on purchase/construction of the house. Further, certain clarifications have also been issued in this regard. These have been summarized as under:

i. *House includes part of the house*: House property does not mean a complete independent house. It includes independent residential units also, like flats in a multi-storeyed complex. The emphasis is not on the type of the property, but, on the head under which the rental income is assessed. [*CIT* (*Addl.*) v *Vidya Prakash Talwar* (1981) 132 ITR 661 (Del)].

ii. *Release deed may also be treated as purchase*: Where a property is owned by more than one person and the other co-owner or co-owners release his or their respective share or interest in the property in favour of one of the co-owners, it can be said that the property has been purchased by the releasee. Such release also fulfils the condition of section 54 as to purchase so far as releasee-assessee is concerned [*CIT* v *T.N. Aravinda Reddy* (1979) 120 ITR 46 (SC)]

iii. *Addition of floor to the existing house eligible for exemption under section 54*: The assessee sold his residential property and invested the capital gain within the stipulated time in the construction of a new floor on another house owned by him by demolishing the existing floor, it was held that he was entitled to exemption under section 54. [*CIT* v *Narasimhan* (*PV*) (1990) 181 ITR 101 (Mad)].

iv. *No exemption under section 54 if land only is sold*: The house property concerned must be building or land appurtenant to building. The basic test was whether the land appurtenant to building could be used independent of the user of the building. If so, it cannot be said to be land appurtenant to building. Further, the basic requirement is that the capital gain should arise from the transfer of building or land, the income of which is chargeable under the head Income from house property. If the land alone is sold, the provisions of section 54 will have no application inasmuch as the income from land is not chargeable under the head Income from house property. [*CIT* v *Zaibunnisa Begum* (1985) 151 ITR 320 (AP)].

v. *Successor is entitled to benefit of exemption in case of death of the assessee*: In case of assessee's death during the stipulated period, benefit of exemption under section 54(1) is available to legal representative if the required conditions are satisfied by the legal representative. [*Ramanathan* (*CV*) v *CIT* (1980) 155 ITR 191 (Mad)].

vi. *Purchase of limited interest in the house eligible for exemption under section 54*: Where an assessee had sold the residential house and acquired only 15% interest in another house and such other house was already used for residence prior to purchase, it was held that the benefit should be available to the assessee. [*CIT* v *Chandaben Maganlal* (2000) 245 ITR 182 (Guj)]. In coming to the conclusion, the High Court followed its own earlier decision in *CIT* v *Tikyomal Jasanmal* (1971) 82 ITR 95 (Guj). In that case, what was purchased was a unit of house property, while in the present case before the High Court, it was a limited interest in the property.

vii. *Construction in another property not eligible for exemption*: An assessee gifted some land to his wife. He, thereafter constructed a building on the said land. The Government acquired the land and building and paid compensation for land to the wife and for the building to the assessee (husband). It was held that capital gain on land was assessable in the hands of the husband by virtue of section 64 but he was not entitled to exemption under section 54 in respect of capital gain on the acquisition of the land of the wife as the capital gain to the wife did not arise on transfer of a residential house. [*T.N. Vasavan* v *CIT* (1992) 197 ITR 163 (Ker)].

viii. *House of the firm used by partners*: Where a firms property is used for residence of partners and thereafter distributed to the partners upon dissolution of the firm and the partner sells the same, exemption can be claimed by the partner under section 54. For this purpose, period for which this property was held by the firm shall also be taken into account for determining the question whether the house property in exemption was a long-term capital asset or not. [*CIT* v *M.K. Chandrakanth* (2002) 258 ITR 14 (Mad)].

ix. *There can be both purchase and construction*: Where the assessee had partly invested the capital gains on the purchase of another house and partly on the construction of additional floor to the house so purchased within the prescribed time limit, it was held that the Income-tax Officer was not justified in restricting exemption to investment on purchase only, holding that the exemption under section 54 was admissible either for purchase or for construction but not for both. [*Sarkar* (*B.B.*) v *CIT* (1981) 132 ITR 661 (Del)].

x. *Construction can start before the sale of asset*: The construction of the new house may start before the date of transfer, but it should be completed after the date of transfer of the original house. [*CIT* v *J.R. Subramanya Bhat* (1987) 165 ITR 571 (Karn)]. The very fact that purchase of another house as also the construction can take place before the sale means that cost of purchase or new construction need not flow from the sale proceeds of the old property. [*CIT* v *H.K. Kapoor* (*Decd*) 1998 234 ITR 753 (All) and *CIT* v *M. Vasudevan Chettiar* (1998) 234 ITR 705 (Mad)].

xi. Allotment of a flat by DDA under the Self-Financing Scheme shall be treated as construction of the house [Circular No. 471, dated 15-10-1986]. Similarly, allotment of a flat or a house by a cooperative society, of which the assessee is the member, is also treated as construction of the house

xii. [Circular No. 672, dated 16-12-1993]. Further, in these cases, the assessee shall be entitled to claim exemption in respect of capital gains even though the construction is not completed within the statutory time limit. [*Sashi Varma* v *CIT* (1997) 224 ITR 106 (MP)]. Delhi High Court has applied the same analogy where the assessee made substantial payment within the prescribed time and thus acquired substantial domain over the property, although the builder failed to hand over the possession within the stipulated period. [*CIT* v *R.C. Sood* (2000) 108 Taxman 227 (Del)].

xiii. As per a circular of CBDT, the cost of the land is an integral part of the cost of the residential house, whether purchased or constructed. [Circular No. 667, dated 18-10-1993].

xiv. Where an assessee who owned a house property, sold the same and purchased another property in the name of his wife, exemption under section 54 shall be allowable. **[*CIT* v *V. Natarajan* (2006) 154 Taxman 399 (Mad)]**.

xv. Where the assessee utilised the sale consideration for other purposes and borrowed the money for the purpose of purchasing the residential house property to claim exemption under section 54, it was held that the contention that the same amount should have been utilised for the acquisition of new asset could not be accepted. [*Bombay Housing Corporation* v *Asst. CIT* (2002) 81 ITD 454 (Bom).

Also followed in ***Mrs. Prema P. Shah, Sanjiv P. Shah* v *ITO* (2006) 282 ITR (AT) 211 (Mumbai)**].

xvi. Where non-resident Indian sold property in India and purchased residential property in U.K. and claimed deduction under section 54, it was held that it was not necessary that residential property showed be purchased in India itself. **[*Mrs. Prema P. Shah, Sanjiv P. Shah* v *ITO* (2006) 282 ITR (AT) 211 (Mumbai)]**. **But, After the Amendment vide Finance (No.2) Act, 2014, exemption is no longer allowed on Investment in residential house outside India.**

b) *Capital gain on transfer of land used for agricultural purposes [Section 54B]*:

Any capital gain (short-term or long-term), arising to an assessee (only individuals), from the transfer of any agricultural land which has been used by the assessee or his parents for at least a period of 2 years immediately preceding the date of transfer, for agricultural purposes, shall be exempt to the extent such capital gain is invested in the purchase of another agricultural land within a period of 2 years after the date of transfer to be used for agricultural purpose, provided the new agricultural land purchased, is not transferred within a period of 3 years from the date of its acquisition.

Section 54B is applicable only to individuals and not to any other assessee this is because the section uses the expression used by "his or a parent of his" which clearly indicate that the "assessee" refers to an individual. [*CIT* v *Devarajalu* (*G.K.*) (1991) 191 ITR 211 (Mad)].

c) *Capital gain on transfer of long-term capital assets not to be charged on investment in certain bonds [Section 54EC]*:

Any long-term capital gain, arising to any assessee, from the transfer of any capital asset on or after 1-4-2000 shall be exempt to the extent such capital gain is invested within a period of 6 months after the date of such transfer in the long-term specified asset provided such specified asset is not transferred or converted into money within a period of 3 years from the date of its acquisition.

Exemption under section 54EC not available in respect of deemed capital gains on amount received on liquidation of a company: Section 54E (now section 54EC) permits reinvestment benefit, if the sale proceeds/capital gains on sale of long-term capital assets are invested in the manner required by the section. Where a shareholder is made liable for deemed capital gains on amount received on liquidation of a company, is he eligible for reinvestment benefit under section 54E (now 54EC)? It was held that section 54E (now 54EC) would have application only where there is an actual transfer and not in a case, where there is only a deemed transfer. [*CIT* v *Ruby Trading Co. Pvt. Ltd.* (2003) 259 ITR 54 (Raj)].

Benefit under section 54EC, etc. available even on transfer of depreciable assets: Although as per section 50 the profit arising from the transfer of depreciable asset shall be a gain arising from the transfer of short term capital asset, hence short-term capital gain but section 50 nowhere says that depreciable asset shall be treated as short-term capital asset. Section 54E [or say 54EC or 54F, etc.] is in independent provision which is not controlled by section 50. If the conditions necessary under section 54E are complied with by the assessee, he will be entitled to the benefit envisaged in section 54E, even on transfer of depreciable assets held for more than 36 months. [*CIT* v *Assam Petroleum Industries* (*P.*) *Ltd.* (2003) 131 Taxman 699 (Gau). See also *CIT* v *ACE Builders Pvt. Ltd.* (2005) 144 Taxman 855 (Bom)].

On the same analogy benefit under section 54EC or 54F shall be available in the case of depreciate asset if these are held for more than 36 months.

- ***RECENT AMENDMENTS IN THE FINANCE (NO.2) ACT, 2014:***

Earlier due to Various Decision of Courts celling limit of Rs. 50Lakh was taken as per financial year. Because the words used in proviso to Section 54EC is "any financial year" and not "relevant financial year".

This means that the assessee cannot invest more than Rs. 50 lacs during on financial year under 54EC bonds but he can do so in two different financial years provided that the financial year falls within the six months time limit after the sale of asset.

- **Reliance is placed on:**

Aspi Ginwala v. Asstt. CIT [2012] 20 taxmann.com 75 (Ahd. - Trib.)

But, After the Amendment vide Finance (No.2) Act, 2014 The investment in capital gains bonds for section 54EC exemption is now being restricted to Rs.50 lakh both in the year of transfer of the capital asset and in the subsequent year, so that one can't claim exemption of Rs.100 lakh for investments made in both the years.

The above amendment has taken effect from **01.04.2014**

d) <u>*Capital Gain on transfer of asset, other than a residential house [Section 54F]*</u>:

Any long-term capital gain, arising to an individual or HUF, from the transfer of any capital asset, *other than residential house property*, shall be exempt in full, if the entire net sales consideration is invested in purchase of one residential house within one year *before* or two years *after* the date of transfer of such an asset or in the construction of one residential house within three years after the date of such transfer. Where part of the net sales consideration is invested, it will be exempt proportionately.

The above exemption shall be available only when the assessee does not own *more than one residential* house property *on the date of transfer* of such asset exclusive of the one which he has bought for claiming exemption under section 54F.

Section 54 and 54F are comparable in many respects. Hence, the law and precedents relating to section 54 as to whether the house property on which investment is made is residential or not, the law relating to time limits, the precedent that construction could start earlier though completed within three years are all equally applicable for section 54F. Hence, for judicial decisions for section 54F, refer to the judicial decisions given under section 54.

11.11 CAPITAL GAIN ON THE TRANSFER OF LAND, FORMING PART OF BUILDING WHICH IS DEPRECIABLE, CAN BE LONG-TERM

Section 50 provides for determination of the cost of construction of superstructure and it does not apply to land as land is not a depreciable asset. Hence, if the building comprising of the land is sold, the capital gain on superstructure shall be short-term capital gain in terms of section 50 and the capital gain on land, if held for more than 36 months, shall be long-term capital gain. This is because the land is independent and identifiable capital asset and it continues to remain so even after construction of the building thereon. [*CIT* v *CITI Bank NA* (2003) 261 ITR 570 (Bom)].

11.12 BLOCK OF ASSETS – SECTION 2(11).

Where land and building were used for the business, an important issue arises whether the new constructed area received can be added to the block of assets. The new constructed area will not be a building used for the purpose of the business. If it is not an asset which will be used as a "Building" for the purpose of business, it may not become a part of the Block of Assets.

For the purpose of redevelopment, the old building has to be demolished. Such building may be part of the block of asset. Issue arises as to whether indexed cost of structure can be deducted to arrive at the long term capital gains on the sale of land. Indexation u/s. 48 is allowed only in respect of cost of acquisition or cost of improvement of the capital asset transferred. Therefore, one may contend that only the land is transferred and not the building, which will be demolished to enable the development of land, hence the cost of structure cannot be taken into consideration and only index cost of land will be considered.

12. INCOME FROM HOUSE PROPERTY

The annual value of property consisting of any buildings or lands appurtenant thereto of which the assessee is the owner, other than such portions of such property as he may occupy for the purposes of any business or profession carried on by him the profits of which are chargeable to income-tax, shall be chargeable to income-tax under the head "Income from house property".

HOW TO COMPUTE INCOME FROM HOUSE PROPERTY

	Rs.
Gross Annual Value	xxxx
Less: Municipal Taxes	xxxx
Net Annual Value	xxxx
Less: Deduction u/s 24	
- Standard Deduction @ 30%	xxxx
- Interest from Borrowed Capital	xxxx
Income From House Property	**xxxx**

Points to remember:

- Annual value of property is chargeable under the head '*Income from house property*'. In order that the annual value be charged under this head, it is *irrelevant* whether the actual income from such house property has accrued or has been received by the assessee.

- Property should consist of any buildings or lands *appurtenant* thereto.

- Section 22 is not confined only to house property, but extends to all buildings whether used as dwelling house or for other purposes {*CIT* v. *Chennai Properties & Investments Ltd.* [2004] 136 Taxman 202 (Mad.); [2002] 266 ITR 685 (Mad.)}.

- The manner in which the building is used by the assessee is not relevant. It can be used by him for letting out on rent, leasing it out, using it for his own residence, etc. However, the building should not be occupied by the assessee for his business or profession. Similarly, the person to whom the building has been let out may use it for any purpose, say, for his own residence or for his business or profession, etc. Further, building may take any form, e.g., a cinema theatre, an auditorium or even an amphitheatre (which does not have a roof).

- Annual value of a building situated *outside India* is also taxable under this head. In the case of a resident but not ordinarily resident or a non-resident, annual value of such a building is charged to tax in India only if income from such property is received or is accrued in India during the previous year.

- Land appurtenant to a building consists of such portions of land that are taken to be a part and parcel of the building in order to *enable the enjoyment* of the possession of such building. Therefore, garden attached to the building, approach roads, etc., form part of the building.

- 'Building' does not include *vacant land*. Thus, income from vacant land is charged either under the head 'Profits and gains of business or profession' or under the head 'Income from other sources', as the case may be.

- The assessee should be the owner of such property.

- The house property should not be *occupied* by the assessee for the purposes of his business or profession, the profits of which are *chargeable* under the head 'Profits and gains of business or profession'

- Income received from giving the building to other person on hire or by license *need not always* be treated under the head 'Income from house property'. Each case has to be looked at from a businessman's point of view to find out whether the letting was the *doing of a business* or the *exploitation of his property* by an owner {*Sultan Brothers (P) Ltd.* v. *CIT* [1964] 51 ITR 353 (SC)}. If it is the doing of a business, the relevant income will be charged under the head 'Profits and gains of business or profession'.

- Interest on Borrowed Capital (of the current year and pre- construction period) is deductible. However, the maximum deduction available if the capital is borrowed on or after 1999 is Rs. 150000 and Rs. 30000 if capital is borrowed before 1.04.1999.

- If the actual rent being in excess of Municipal Corporation/standard rent, all the expenses and outgoings have to be excluded from the rent receivable and the net of the amount should be considered to be the income of the Assessee**.** *(ITO V. GOPICHAND P. GODHWANI (2005) 1 SOT 374 (MUM.))*

- *Where assessee, co – owner of house property, claimed deduction on account of salary and bonus of sweepers, pumpman and liftman and electricity charges being expenses incurred for electric burning for pump motor and common passage, assessee was not entitled to deduction u/s 24; however, annual value of assessee's house property should be assumed at reduced value, i.e., after deducting impugned amounts from rental, being only in relation to expenditure required to be necessarily incurred for enjoyment / user of relevant property.*

J.B. PATEL CO. V.S DY. CIT (ASSTT.) (2009) 118 ITD 556 (AHD.)

- In the case of **M.V. SONAVALA V. CIT, 177 ITR 246 (BOM),** it was held that "*the income from house property has to be computed on the basis of the sum of which the property might reasonably be let from year to year to the annual Municipal rateable value. The word "or" is disjunctive as such it is possible to take the sum for which property might reasonably let from year to year or the Municipal rateable value. It is pertinent to note that while deciding this issue the Hon'ble jurisdictional High court took into consideration the decisions of the Apex Court rendered in the case of Devan Daulat Rai Kapoor Vs. New Delhi Municipal Committee, 122 ITR 700 (SC) and in the case of Sheila Kaushish vs. CIT, 131 ITR 435 (SC).*"

13. <u>SECTION 43CA OF THE INCOME TAX ACT, 1961:</u>

Special provision for full value of consideration for transfer of assets other than capital assets in certain cases.

43CA (1) *Where the consideration received or accruing as a result of the transfer by an assessee of an asset (other than capital asset), being land or building or both, is less than the value adopted or assessed or assessable by any authority of a state government for the purpose of payment of stamp duty in respect of such transfer, the value so adopted or assessed or assessable shall, for the purpose of computing profits and gains from such transfer of such asset, be deemed to be the full value of the consideration received or accruing as a result of such transfer.*

(2) The provisions of sub-section (2) and sub-section (3) of section 50C shall, so far as may be, apply in relation to determination of the value adopted or assessed or assessable under sub-section (1).

(3) Where the date of agreement fixing the value of consideration for transfer of the asset and the date of registration of such transfer of asset are not the same, the value referred to in sub-section (1) may be taken as the value assessable by any authority of a state government for the purpose of payment of stamp suty in respect of such transfer on the date of agreement.

(4) The provisions of sub-section (3) shall apply only in a case where the amount of consideration or a part thereof has been received by any mode other than cash on or before the date of agreement of transfer of the asset.

Existing provision in respect of the above amendment:

The White paper on Black Money presented by the Government of India points out that very high levels of stamp duty (over 5%) in many states create incentives for tax evasion through under reporting of consideration in sale deed.

To combat tax evasion through under reporting of sale consideration in sale deed, section 50C was inserted in the Act by the Finance Act, 2002 w.e.f. 01.04.2003.

In cases of transfer of capital asset being land or building or both, the said section deems stamp duty value as the full value of consideration where the consideration shown in the sale deed is less than the stamp duty value.

Currently, when a capital asset, being immoveable property, is transferred for a consideration which is less than the value adopted, assessed or assessable by any authority of a state government for the purpose of payment of stamp duty in respect of such transfer, then such value (stamp duty value) is taken as full value of consideration under section 50C. These provisions do not apply to transfer of immoveable property, **held by the transferor of stock in trade.**

Loopholes/Problems:

In CIT vs. Kan Construction and Colonizers (P) Ltd. [2012 20 taxmann.com 381] , the Allahabad High Court held that Section 50C is not applicable to sale of plots by a builder since plots are his stock in trade and not capital assets in view of the following:

- Section 50C uses the word "capital asset". For applicability of section 50C, one of the essential requirements is that land or buildings sold should be capital asset. Stock in trade has been excluded from the definition of capital asset by section 2(14).
- Investment in purchase and sale of plots by a builder who is indulged in selling buildings is ancillary and incidental to his business activity. 'Stock in trade' includes all such chattels as are required for the purpose of being sold or let to hire on a person's trade.

To overcome the judicial decision in Kan Construction (supra), the Finacne Act, 2013 inserted new section 43CA with effect from assessment year 2014-2015.

14. SECTION 194-IA OF THE INCOME TAX ACT, 1961

Another amendment is in respect of payment on transfer of certain immoveable property other than agricultural land.

194-IA *(1) Any person, being a transferee , responsible for paying (other than the person referred to in section 194LA) to a resident transferor any sum by way of consideration for transfer of any immoveable property (other than agricultural land) shall, at the time of credit of such sum to the account of the transferor or at the time of payment of such sum in cash or by issue of a cheque or draft or by any other mode, whichever is earlier, deduct an amount equal to one per cent of such sum as income tax thereon.*

(2) No deduction under sub-section (1) shall be made where the consideration for the transfer of an immoveable property is less than fifty lakh rupees.

(3) The provisions of section 203A shall apply to a person required to deduct tax in accordance with the provisions of this section.

Explanation.- *For the purpose of this section,-*

(a) "agricultural land" means agricultural land in India, not being a land situated in any area referred to in items (a) and (b) of sub-clause (iii) of clause (14) of section 2;

(b) "immoveable property" means any land (other than agricultural land) or any building or part of a building.

Under Section 195, on transfer of immoveable property by a non-resident, tax is required to be deducted at source by the transferee. However, there is no such requirement on transfer of immoveable property by a resident except in case of compulsory acquisition of certain immoveable properties (section 194LA).

The Finance Act, 2013 inserted new section 194-IA to introduce TDS on consideration on transfer of immoveable properties.

The objects of this have been explained by Explanatory Memorandum as under:

"*There is a statutory requirement under section 139A of the Income Tax Act read with rule 114B of the Income Tax Rules 1961 to quote Permanent Account Number (PAN) in documents pertaining to purchase or sale of immoveable property for value of Rs.5 lakh or more. However, the information furnished to the department in Annual Information Returns by the Registrar or Sub-Registrar indicate that a majority of the purchasers or sellers of immoveable properties, valued at Rs.30 lakhs or more, during the financial years 2011-2012 did not quite or quoted invalid PAN in the documents relating to transfer of property. In order to have a reporting mechanism of transaction in the real estate sector and also to collect tax at the earliest point of time, it is proposed to insert a new section 194-IA…"*

The Finance Minister in his speech explained the objects of the new section 194-IA as under:

"145. Transactions in immoveable properties are usually under valued and under reported. One-half of the transactions do not carry the PAN of the parties concerned. With a view to improve the reporting of such transactions and the taxation of capital gains, I propose to apply TDS at the rate of one percent on the value of transfer of immoveable property where the consideration exceeds Rs.50 lakhs. However, agricultural land will be exempt."

Section 194-IA provides that every transferee (purchaser or buyer), at the time of making payment or crediting of any sum as consideration for transfer of immoveable property (other than agricultural land) to a resident transferor, shall deduct tax, at the rate of 1% of such sum. In order to reduce the compliance burden on small taxpayers, no deduction of tax shall be made where the total amount of consideration for the transfer of an immoveable property is less than Rs.50,00,000. The provisions of section 203A [regarding obligation of deductors to obtaining tax deduction and collection account number (i.e. TAN) shall not apply in respect of tax deducted under this section. This amendment will take effect from 01.06.2013.

15. IMPECT OF ICDS ON THE REVENUE RECOGNITION BY THE REAL ESTATE DEVELOPER

- **Applicability of Accounting Standard-7 "Construction Contract" on the Builder/Real estate Developer**

The ICAI has prescribed Accounting Standard No. 7 "Construction Contract" in which accounting of Construction contractor described.

The Method of Recognition of revenue provided under the A.S. 7 is as follow

- **Before 2002**

Pre-2002 AS-7 (Old) dealing with Construction Contracts permitted two methods for revenue recognition, namely, Percentage of Completion Method (POCM) and Completed Contract Method (CCM). So before 2002 construction contractor can follow either POCM or CCM method for the recognition of revenue under the Income tax.

- **After 2002**

Thereafter accounting standard was revised by the Institute of Chartered Accountant of India and which permits only one method i.e. Percentage of Completion Method has been implemented by the construction industry at large and is also accepted by the tax authorities. Accordingly, the use of completed contract method is no longer permitted to construction contractor

Thereafter Recently CBDT (Central Board of Direct Tax) notified 10 ICDS (Income disclosure and computation slandered) for the computation of taxable income/Losses which is applicable from the financial year 2015-16 i.e. A.Y. 2016-17 and assessee is required to mandatory follow these standard for the computation of the income.

Out of these ICDS the ICDS No. III is related to "Construction Contract" wherein the computation of taxable income of the Construction Contract is provided.

The Method of Recognition of revenue provided under the ICDS III is as follow:-

Section 145(1) – Income chargeable under the heads "Profits and Gains from Business or Profession" or "Income from other Sources" – subject to 145(2)- as per method of accounting regularly followed

 Section 145(2) – the Central Government has power to notify "ICDS"

 CBDT vide notification dated 31 March 2015 introduced 10 ICDS to be effective from 1 April
2015 and shall be accordingly apply for AY 2016-17 onwards.

Section 145(3)-AO has the power to make best judgement assessment u/s. 144 if he is not satisfied about the :-

o correctness or completeness of the accounts of the assessee ; or
o method of accounting is not regularly followed ;or
o Income not computed as per ICDS

 Hence ICDS has to be mandatorily followed or else best judgement assessment can be done by Assessing Officer.

Under the ICDS III the method of recognition of revenue by the Contractor is same as per revised AS 7. So under this ICDS it is mandatory requirement to follow the Percentage of Completion method for the recognition of revenue.
So as per revised AS-7 and ICDS III, after 2002 it is clear position that assessee under construction contract it is required to follow the percentage of completion method for the recognition of revenue.

But, the question is arise weather the ICDS III and AS-7 applicable on the Real Estate Developer or not.

Background of AS -7

The ICAI issued Accounting Standard (AS) 7 – 'Construction Contract' in the year 1983 which was later on revised in the year 2002. The AS 7 laid down the principles of accounting for 'construction contracts' in the financial statements of the Contractors. As per the revised AS 7 the accounting was to be done as per percentage/progressive completion method.

In response to a query rose, on applicability of revised AS 7 to a real estate developer, before the Expert Advisory Committee (EAC) formed by the ICAI, the EAC observed that the pre revised AS 7 specifically mentions about its applicability to enterprises undertaking construction activities on their own which would include real estate developer. However, the revised AS 7 is applicable only to Contractors.

- **The Scope of AS -7 before the revision in year 2002 is as follows**

"This Statement deals with accounting for construction contract in the financial statement of enterprise undertaking such contract (hereinafter referred to as "Contractor") this statement will also apply to enterprise undertaking construction activities of the type dealt with in this statement not as contractor but on their own account as a venture of commercial nature where the enterprise has entered into agreement for sale".

As per above before 2002 the AS -7 was applicable on the both contractor and Real estate developer who develop the building and thereafter sale on their own account.

- **The Scope of AS-7 after the revision in year 2002 is as follows**

"The Standard should be applied in accounting for construction contract in the financial statement of Contractor"

As per the revise AS -7 the scope of the standard was limited to contractor only. So after revision a real estate developer/ Builder are not covered under the AS -7, accordingly they are not required to follow the percentage of completion of method for the revenue recognition.

- **The Scope of ICDS III is as follows**

"This Computation and Disclosure should be applied in determination of income for a construction contract for a contractor"

- **Applicability of ICDS III**

Meaning of Construction contract as given in ICDS is as follow

2(1)(a) A "construction contract" is a contract specifically negotiated for the construction of an asset or a combination of assets that are closely interrelated or interdependent in terms of their design, technology and function or their ultimate purpose or use and includes :

(i) Contract for the rendering of services which are directly related to the construction of the asset, for example, those for the services of project managers and architects;

(ii) Contract for destruction or restoration of assets, and the restoration of the environment following the demolition of assets.

So the ICDS apply on **Construction Contractor** and to service providers such as architects, project managers, etc. who generally, render services which are directly related to the construction contract. These categories of taxpayers will now be mandatorily required to compute their taxable income on POCM basis.

However this ICDS is silent whether the same is applicable to Real Estate Developers or not. But if we see applicability of ICDS – III then it will apply only on construction contract and service provider who is providing the service related to the construction contract and the Scope of ICDS III it also similar to AS -7 and as per various decided case law it is decided that provision of AS -7 is not applicable on Real Estate Developer because of that it seems that there is no applicability of ICDS III on Real estate Developer and accordingly the mandatory requirement to follow the percentage of completion method for recognition of revenue under ICDS III will not applicable on Real estate developer. However matter may be go for litigation.

Attention should be also paid on the following relevant decided Judgments

Revised Accounting Standard 7 – 'Construction Contract' is applicable to only contractors and not to builders and real estate consultants. Accordingly, the Project Completion Method consistently followed by the taxpayer for recognizing revenue in the books of accounts cannot be regarded as an unreasonable.	*Unique Enterprises v. ITO [2010-TIOL -737-ITAT-MUM*
The Delhi High Court in the case of CIT v. Smt. V. Sikka [1984] 149 ITR 73 has entertained a view that even for the first year, the method of accounting is deemed to have been employed if the same is shown to have been regularly employed in subsequent years as is also the case in appeal. The real estate developer is not a pure contractor but is a seller of flats/goods. It is not mandatory for all real estate developers to follow percentage completion method as prescribed by Institute of Chartered Accountants of India under AS-7.	*CIT v. Smt. V. Sikka [1984] 149 ITR 73* *Delhi High Court*
The Delhi High Court in the case of CIT v. Manish Buildwell (P.) Ltd. [IT Appeal No. 928 of 2011, dated 15-1-2011] has ruled that Accounting Standard-7 issued by the Institute of Chartered Accountants of India recognizes the position that in the case of construction contracts the assessee can follow either the project completion method or percentage completion method. Neither the revised Guidance Notes 2012 issued by the Institute of Chartered Accountants of India nor the 'Exposure Draft for Guidance Note on recognition of revenue' issued by the Institute of Chartered Accountants of India in 2011 are mandatory. It is the option of the assessee to follow either the completed contract method or the percentage completion method. The completed contract method followed by the assessee, in the instant case, therefore, could not be faulted with by the revenue authorities and on that basis it is neither correct nor justified to say that the accounts did not present correct and complete picture of its profits. The accounts rejected by the Assessing Officer on the basis adopted by him are, thus, not found tenable.	*CIT v. Manish Buildwell (P.) Ltd. [IT Appeal No. 928 of 2011, dated 15-1-2011]* *Delhi High Court*
In the instant case the assessee was engaged in the business of developing and selling real estate projects. It filed nil return of income for both the assessment years 2008-09 and 2009-10, by adopting Project Completion Method. During assessment, the AO rejected the assessee's accounts on the ground that it hadn't followed AS-7 for recognition of revenue as per which income was to be deduced on the basis of Percentage Completion Method. The AO, accordingly, computed the profit on percentage completion method and completed the assessment. Further, CIT (A) upheld the action of action of AO. *On appeal, the Tribunal held in favour of assessee as under:* *1) The assessee maintained complete books of account, which were duly audited by qualified Chartered Accountants. It had also maintained its account on mercantile basis by regularly applying Project Completion Method. The assessee had been consistently followed the same method. The auditors had reported no change in*	*Krish Infrastructure (P.) Ltd. v. ACIT [2013] 35 taxmann.com 38 (Jaipur - Trib.)*

method of accounting adopted by the assessee. *2) The real estate developers are not pure contractors but are sellers of flats or goods. It is not mandatory for all real estate developers to follow Percentage Completion Method as per AS-7 prescribed by ICAI. The AS-7 recognizes the position that in the case of construction contracts the assessee could follow either the Project Completion Method or Percentage Completion Method.;* *3) The Apex Court in the case of CIT v. Hyundai Heavy Industries Co. Ltd., [2007] 161 Taxman 191 (SC) also took the similar view and held that both the methods of accounting (i.e., Project Completion Method and Completed Contract method) were recognized methods of accounting. The assessee was at liberty to choose any of the above methods and if any one of the method of accounting was consistently followed by the assessee, the AO couldn't change such method of accounting.* *4) The completed contract method followed by the assessee, in the instant case, therefore, could not be faulted with by the revenue authorities and on that basis it was not correct to say that the accounts of assessee did not present correct and complete picture of its profits.* *5) Therefore, there was no justification in rejection of accounts by application of provisions of section 145(3) and changing the method from project completion to percentage completion method by the AO, which was upheld by the CIT (A). Therefore, the order of the Commissioner (Appeals) was to be set aside*	

The ICDS III does provide the clear contention that whether it will apply on real estate developer or not and further some professional has also applied this issue to CDBT. So at present if we see as per law then it seems that ICDS III will not apply on the Real estate Developer accordingly it will not mandatory requirement on real estate developer to follow percentage of completion method. However in future CBDT may decide this issue.

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